

**A COMPARATIVE REAPPRAISAL OF DEBT RELIEF
MEASURES FOR NATURAL PERSON DEBTORS IN SOUTH
AFRICA**

By

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VOORWOORD

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SUMMARY

The purpose of this thesis is to do a comparative reappraisal of debt relief measures available to natural person debtors in the South African insolvency law. Although the broader South African natural person insolvency system currently includes three statutory debt relief procedures, namely, the sequestration procedure regulated by the Insolvency Act 24 of 1936, the administration order procedure in terms of the Magistrates' Courts Act 32 of 1944 and the debt review procedure found in the National Credit Act 34 of 2005, not all natural person debtors have access to the system. The majority of this marginalised group are debtors with no income and no assets (the so-called No Income No Asset (NINA) debtors). Also, only one measure provides real debt relief in the form of a statutory discharge of debt. Furthermore, the existing measures have developed in a haphazard fashion which has led to a multiplicity of procedures, regulators and forums that resulted in ineffectiveness, inequality and uncertainty. The larger system therefore lacks proper policy considerations.

This thesis provides the reasons for reform by, amongst others, arguing that the present situation is unconstitutional as it unreasonably and unfairly discriminates against the NINA group of debtors in particular. It measures the broader South African system against internationally accepted principles of efficient and effective natural person insolvency regimes. In this regard it is found that the system as a whole is seriously deficient. With reference to international principles and guidelines as well as suitable attributes found in foreign jurisdictions, the thesis concludes with suggestions for real law reform. Both substantive and procedural recommendations are made.



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CHAPTER 1: INTRODUCTION

SUMMARY

- 1.1 Research motivation
 - 1.2 Research objectives
 - 1.3 Delineation and limitations
 - 1.4 Methodology
 - 1.5 Chapter overviews
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Consumer debts however are no problem per se: they are one of the great dynamic factors in our economies.¹ A high level of domestic consumption is required for both stability and growth. This is why consumers are encouraged by governments to consume. One of the ways to boost this consumption is to facilitate and expand credit facilities for consumers. Consumer debts become a problem when debtors are unable to find solutions for repayment without professional help and that is why society as a whole bears a collective responsibility.²

1.1 Research motivation

The South African government appreciates the sentiment that society as a whole bears a collective responsibility in instances where large credit providers are faced with financial difficulty, but not in case of natural person insolvency. This phenomenon is best illustrated by the measures implemented in 2014 to curb the financial difficulties of African Bank,³ the largest provider of unsecured credit in South Africa.⁴ On 10 August 2014 its financial woes became that of the broader South African society as the South African Reserve bank⁵ decided to split the bank into a 'good bank' and a 'bad bank' and to bail out the 'bad' one. The 'good bank'

¹ See also Ramsay 2006 *U III L Rev* 244–245 and Cork *Report* par 9. In the Cork *Report*, credit is described as 'the lifeblood of the modern industrialised economy'.

² INSOL *Consumer debt report* I 4. See also Cork *Report* para 23 and 198 on the responsibility that rests on society to provide adequate insolvency laws.

³ African Bank is listed as ABL on the Johannesburg stock exchange.

⁴ Fin24 *African Bank fined R20m for reckless lending* <http://bit.ly/Mwy8AR> (accessed 27 December 2014).

⁵ Hereafter 'the Sarb'.

was recapitalised and the 'bad bank' incorporated in a vehicle supported by the Sarb. The latter does not form part of African Bank anymore. The Sarb, and therefore the greater South African society, has thus bought a substantial portion of the 'non- and under-performing assets' and other 'high risk loans' in order to separate the 'two banks'.⁶ The then governor of the Sarb, Gill Marcus, made the following statement at the time:⁷

Sarb in consultation with the Minister of Finance, has decided to implement a number of support measures ... This will further strengthen the resilience of the banking system as a whole, and importantly, they will provide African Bank with the best chance of a viable future.

She also emphasised that⁸

[c]ollection against the bad book will be continued, and indeed strengthened: There is no payment holiday for anyone owing a loan from African Bank.

The importance of supporting a financial institution to provide it 'with the best chance of a viable future', is thus recognised in South Africa. This is despite African Bank's own culpability regarding its financial difficulties.⁹ The bank was presumably bailed out as the failure of such a large financial institution would cost the South African economy, and therefore the larger society, even more and therefore the measures taken make business sense. However, the two quoted statements by Marcus illustrate the contrasting views that the South African society, or at the very least government and the financial sector, apparently hold on the insolvency of too-big-to-fail credit providers *versus* that of individuals. This is so since it ostensibly makes sense to rescue a large credit provider in order to provide it 'with the best chance of a viable future', but not necessarily to assist the individuals who became over-

⁶ Fin24 *African Bank placed under curatorship* <http://bit.ly/1reuxWp> (accessed 27 December 2014).

⁷ *Ibid.*

⁸ *Ibid.*

⁹ See Fin24 *African Bank kept lending to indebted customers* <http://bit.ly/1A23y7Z> (accessed 27 December 2014) for some of the reports on the reckless behaviour of the bank in contravention of the National Credit Act 34 of 2005. See ch 5 par 5.5 on the National Credit Act's reckless credit provisions. See also African Bank's statement as a response to the R300m fine that the National Credit Regulator (hereafter 'the NCR') imposed on the Bank for its reckless behaviour. In the statement African Bank described the NCR's fine as being without a 'rational basis' – African Bank Investments Limited *African Bank fine verges on overkill* <http://bit.ly/1L7EhN7> (accessed 27 December 2014). The fine was later reduced by settlement to R20m. See Fin24 *African Bank fined R20m for reckless lending* <http://bit.ly/Mwy8AR> (accessed 27 December 2014).

indebted due to, amongst others, the reckless behaviour of this very credit provider. In contrast, collection measures against the 'bad book', which evidently includes a large percentage of over-indebted individuals, 'who are unable to find solutions for repayment' have been stepped up.¹⁰ However, to collect more aggressively on these debts will only pose a real and enduring problem to affected insolvent clients (who are effectively in the same position as the bank) if they do not have safety nets (similar to those that government and therefore indirectly the larger South African society has thrown out to African Bank) available to them. Therefore, the African Bank debacle does not only tell the story of a too-big-to-fail financial institution, but also brings to light the question of whether South African natural person insolvents also have access to sufficient and efficient debt relief measures to afford them 'with the best chance of a viable future'. This is the focal point of this thesis.

The South African insolvency system provides for three statutory natural person debt relief measures that stem from various pieces of legislation. These are the sequestration procedure provided for by the Insolvency Act,¹¹ the administration order procedure in terms of section 74 of the Magistrates' Courts Act¹² and the debt review procedure regulated by section 86 of the National Credit Act.¹³ The sequestration procedure is in essence an asset liquidation procedure whereas the administration order and debt review procedures generally take the form of court sanctioned repayment plans. However, only one of these measures, namely, the sequestration procedure, provides for real debt relief in the form of a statutory discharge of pre-insolvency debt.¹⁴ Due to its discharge feature, the sequestration procedure is deemed to be the primary South African debt relief measure,¹⁵ despite the fact that debt relief is not the procedure's main aim, but merely a consequence

¹⁰ Moral hazard clearly did not play a decisive role in the Sarb's decision to bail out African Bank as the bank's reckless behaviour played a major role in its own demise (and in that of some of its clients): *ibid.*

¹¹ 24 of 1936. See the discussion of this procedure in ch 3 par 3.3.

¹² 32 of 1944. Both the Insolvency Act and the Magistrates' Courts Act resort under the Department of Justice and Constitutional Development. See the discussion of the administration order procedure in ch 4 par 4.2.

¹³ 34 of 2005 (hereafter 'the NCA'). The NCA resorts under the Department of Trade and Industry. See the discussion of the debt review procedure in ch 4 par 4.3.

¹⁴ S 129 of the Insolvency Act.

¹⁵ See Coetzee and Roestoff 2013 *Int Insolv Rev* 193.

thereof.¹⁶ In order to qualify for this ‘privilege’ (of obtaining a sequestration order and the eventual discharge that it brings about), the applicant has to, amongst others, prove that sequestration will be to the advantage of creditors.¹⁷ As Erasmus J remarked: ‘[T]he whole tenor of the [Insolvency] Act, inasmuch as it directly relates to sequestration proceedings is aimed at obtaining a pecuniary benefit for creditors.’¹⁸ Because of the sequestration procedure’s discharge attribute, the other two statutory debt relief procedures can be regarded as secondary measures. Although these procedures were developed with the object of assisting financially overcommitted individuals, it seems that, because they do not offer a discharge, neither of them was ever intended as a remedy for hopeless financial situations. It rather appears that they were devised to assist only the ‘mildly’ over-indebted during a period of temporary financial misfortune. This is so since the lack of a discharge may subject hopelessly insolvent individuals to repayment terms being extended unconscionably – if they are fortunate enough to qualify for one of the secondary measures. As both of these measures are in essence repayment plans, some level of disposable income, which is susceptible to distribution amongst creditors, is necessary. It can therefore be said, albeit indirectly, that the advantage for creditors’ requirement also forms part of these measures. In this regard, the South African position stands in stark contrast with the world-wide trend to accommodate all honest over-burdened natural person insolvents seeking a solution to their financial difficulties through a discharge of debt,¹⁹ a movement that has its origins in the United States of America’s ‘fresh start principle’.²⁰ This principle was described in *Local Loan Co v Hunt* in the following terms:²¹

[I]t gives to the honest but unfortunate debtor ... a new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of pre-existing debt.

¹⁶ See *Ex parte Ford* 2009 (3) SA 376 (WCC) 383 and *Ex parte Shmukler-Tshiko* 2013 JOL 29999 (GSJ) in general.

¹⁷ See ss 6, 10 and 12.

¹⁸ *BP Southern African (Pty) Ltd v Furstenburg* 1966 (1) SA 717 (O) 720.

¹⁹ See Niemi 2012 *J Consum Policy* 444 and 449 as regards the international trend to provide a discharge which is deemed to be the most important aspect of natural person insolvency law. See also Ziegel 2004–2005 *Penn St Int’ L Rev* 645 who divides systems into categories on the basis of their responsiveness to consumer insolvencies. South Africa can be categorised as very conservative in this regard.

²⁰ See further ch 2 par 2.2.

²¹ 1934 *US* 244.

Over and above the advantage requirement, which serves as the major stumbling block in accessing debt relief measures in South Africa, somewhat more technical requirements further hinder the utilisation of these measures.²² These requirements are mostly found in the two secondary measures. As far as the administration order is concerned, only debtors with R50 000 or less in outstanding debts are allowed access to the procedure; this excludes those with unsettled debt of more than the threshold from its application.²³ The debt review procedure in turn poses a number of requirements which could render it unsuitable in some instances. These are that only credit agreements as defined in the NCA are subject to the procedure²⁴ and that agreements in terms of which credit providers have commenced individual enforcement procedures are excluded.²⁵ Nevertheless, as was mentioned, the most significant differentiating factor as regards those who can access some form of relief and those who cannot, is the advantage for creditors requirement. This direct and indirect requirement has the effect of rendering debt relief to specifically those with no income and no assets (the so-called No Income No Asset (NINA) debtors) extremely difficult.²⁶ It can therefore be said that, in South Africa, a person can be 'too broke to go bankrupt'.²⁷ The last possible resort for excluded debtors is to enter into voluntary negotiations with creditors to agree on debt rearrangements. However, these debtors are obviously not in a position to negotiate as they cannot offer any monetary return to creditors.

From this preliminary outline of the South African statutory debt relief measures it can already be seen that the system seems to be inadequate from a debt relief

²² See Coetzee and Roestoff 2013 *Int Insolv Rev* pt 3 for a detailed discussion of the entry requirements of the individual procedures as well as their cumulative effect.

²³ S 74(1)(b) read together with GN R1411 in GG 19435 of 30 October 1998.

²⁴ See s 4 of the NCA.

²⁵ See s 86(2) of the NCA.

²⁶ Included in this concept are the low income and low assets (the so-called Low Income Low Asset (LILA)) debtors. In 1998, in England, the Department of Constitutional Affairs announced a review of the enforcement of civil court judgments, which amongst others re-evaluated the English administration order scheme. Independent research commissioned by the department identified three types of debtors, namely, the so-called 'could pays', 'can't pays' (i.e. the NINA and LILA debtors) and 'won't pays'— see *A choice of paths* 37. See also McKenzie Skene and Walters 2006 *Am Bankr LJ* 477; Roestoff and Renke 2006 *Obiter* 108 and in general Coetzee and Roestoff 2013 *Int Insolv Rev*.

²⁷ Rochelle 1996 *TSAR* 319.

perspective and that reform is necessary.²⁸ In this regard it is important to acknowledge the research by Roestoff who for the first time conducted a proper holistic assessment of the South African natural person insolvency system from a debt relief perspective. The LLD degree, with a thesis titled *'n Kritiese evaluasie van skuldverligtingsmaatreëls vir individue in die Suid-Afrikaanse insolvensiereg*,²⁹ was awarded to her by the University of Pretoria in 2002. As various developments and occurrences have taken place since this last in-depth appraisal of the system, there is currently a need for a re-evaluation of the system. The developments and occurrences referred to include the promulgation of the NCA which has introduced a new debt relief procedure;³⁰ the great recession of 2007/2008 and the rise in over-indebtedness caused by it;³¹ the latest introduction of international instruments and best practices in response to the recent global economic changes which have not been duly considered in a principled way in South Africa;³² and new versions of the Insolvency Bill which do not seem to address all pertinent issues.³³ Furthermore, the plight of the NINA debtor, which forms a major focus of this thesis, has not been thoroughly considered in the South African insolvency context.

South African insolvency legislation is not entirely stagnant as it is currently in a process of reform. In this regard, various versions of the Insolvency Bill,³⁴ in which an attempt is made to combine personal and corporate insolvency in a single statute, have seen the light over the past fifteen years. However, this reform does not take a

²⁸ See also Boraine and Van der Linde 1998 *TSAR* 621 and 1999 *TSAR* 38; Boraine and Roestoff 2000 *Obiter* 33 and 2000 *Obiter* 241; Boraine and Roestoff 2002 *Int Insolv Rev* 1; Roestoff and Renke 2003 *Obiter* 1; Roestoff and Renke 2005 *Int Insolv Rev* 93; Roestoff and Renke 2005 *Obiter* 561 and 2006 *Obiter* 561; Van Heerden and Boraine 2009 *PELJ* 22; Steyn 2012 *PELJ* 190; Roestoff and Coetzee 2012 *SA Merc LJ* 53; Boraine *et al* 2012 *De Jure* 80 and 2012 *De Jure* 253; Coetzee and Roestoff 2013 *Int Insolv Rev* 188; Boraine and Roestoff 2013 *World Bank legal review* 91; Boraine and Roestoff 2014 *THRHR* 351 and 2014 *THRHR* 527.

²⁹ Directly translated as 'A critical evaluation of South African debt relief measures for individuals in the South African insolvency law'.

³⁰ See further ch 4 par 4.3.

³¹ See below.

³² See ch 2 in general.

³³ See ch 3 and ch 5 par 5.2.

³⁴ The South African Law Commission published a report titled the *Report on the review of the law of insolvency* in 2000. It contained a draft bill as well as an explanatory memorandum – hence the '2000 Insolvency Bill' and '2000 Explanatory memorandum' respectively. The latest versions of the documents are unofficial working copies on file with the author (hereafter 'Bill' or '2015 Insolvency Bill' and '2014 Explanatory memorandum' respectively). This research will mostly refer to the 2015 Insolvency Bill except where it specifically states that the clause referred to is as provided for in the 2000 Insolvency Bill.

holistic approach to re-evaluating all statutory natural person debt relief measures as the administration order and debt review procedures are not considered. Nevertheless, as far as the underlying motif of and consequently access to the sequestration procedure are concerned, the Law Reform Commission has recommended that the advantage for creditors requirement be retained.³⁵ From the latest draft, the 2015 Insolvency Bill, it would appear that the commission has not changed its mind in this regard,³⁶ although it has not expressly indicated its reasons for recommending the retention of this requirement.³⁷ Nevertheless, a novel development with the potential to increase access to the broader system, is the commission's proposal that provision be made for a pre-liquidation³⁸ composition³⁹ with creditors. It has been stated that the measure is indeed supposed to afford debt relief to debtors who are unable to show an advantage for creditors and are therefore excluded from the liquidation process.⁴⁰ It was originally proposed that the procedure be accommodated in the Magistrates' Courts Act,⁴¹ but it has of late been incorporated in the Insolvency Bill. Whether the proposed measure will reach its objective of assisting presently excluded individuals remains to be seen.

Further indications that a reappraisal of the existing system may be necessary stem from South Africans' present levels of over-indebtedness⁴² and some of the socio-economic conditions that we are faced with today. In this regard, the South African economy is regularly described as dual in nature as it contains two different segments, namely, the formal and in some respects ultramodern economy and the 'secondary', underdeveloped economy. There is a weak integration between the two

³⁵ See cls 7(1)(b) and 8(1)(c) of the 2000 Insolvency Bill and the 2000 *Explanatory memorandum* 15.

³⁶ See cls 3(8)(a)(ii), 10(1)(c)(i) and 11(1)(c) of the 2015 Insolvency Bill.

³⁷ However, see 2014 *Explanatory memorandum* 23.

³⁸ The Insolvency Bill uses the term 'liquidation' when referring to both the liquidation of juristic persons and the sequestration of natural persons.

³⁹ The title of the proposed provision is confusing as it could mistakenly be interpreted to require a composition as a pre-condition for insolvency proceedings. See further ch 5 par 5.2.

⁴⁰ See 2014 *Explanatory memorandum* 201.

⁴¹ See 2000 *Explanatory memorandum* and 2000 Insolvency Bill schedule 4. See Roestoff and Jacobs 1997 *De Jure* 204 and 2000 *De Jure* 131 *et seq* for a discussion of the proposal in the 2000 Insolvency Bill.

⁴² Although not a specific focus of this thesis, Ziegel 2004–2005 *Penn St Int'l L Rev* 642–645 notes four general reasons for the rapid growth of over-indebtedness and consequently insolvencies globally. These are 'Rapid growth in the use and availability of consumer credit'; 'Reduction in savings by individuals and families'; 'Financial mismanagement by consumers and lack of financial literacy'; and 'Impact of unforeseen circumstances'.

economies and almost no middle ground.⁴³ This dualism provides for a complex socio-economic environment. Even though South Africa can compare to developed economies in many respects, the other side of the coin looks very different. The latest World Bank⁴⁴ statistics estimate the South African poverty headcount ratio (as a percentage of the population living below the national poverty line) at 53.8% in 2011.⁴⁵ Furthermore, Statistics South Africa⁴⁶ reflects the percentage unemployed persons⁴⁷ at 26.4% for the first quarter of 2015,⁴⁸ which according to the World Bank ranks amongst the highest in the world.⁴⁹ Also, 29% of the total population of 53 701 000 individuals benefited from social grants in 2014 and the percentage of households that have received at least one grant in 2014 were estimated to be around the 44.5% mark.⁵⁰ The number of South Africans liable for personal income tax stands in stark contrast to this figure. Even though the South African Revenue Services⁵¹ reported a growth in the individual tax register from 5.9 to 16.8 million in 2014, following a policy change in 2010 to register all individuals who are formally employed,⁵² the percentage is still low in comparison to the number of individuals who rely on social support. This figure obviously does not reflect the number of individuals actually liable for or paying personal income tax, as all salary earners, irrespective of whether they are liable for individual income tax, must now be registered with the SARS. A more accurate estimate of individuals actually liable for

⁴³ See World Bank *South Africa economic update* <http://bit.ly/17kOerl> (accessed 27 December 2014) in relation to the South African dual economy.

⁴⁴ Hereafter the 'WB'.

⁴⁵ WB *Poverty headcount ratio at national poverty line (% of population)* <http://bit.ly/Y6yHyu> (accessed 25 June 2015).

⁴⁶ Hereafter 'STATS SA'.

⁴⁷ The report defines unemployed persons as those (aged 15–64 years) who:

- (a) Were not employed in the reference week; and
- (b) actively looked for work or tried to start a business in the four weeks preceding the survey interview; and
- (c) were available for work, i.e. would have been able to start work or a business in the reference week; or
- (d) had not actively looked for work in the past four weeks but had a job or business to start at a definite date in the future and were available.

⁴⁸ STATS SA *Quarterly labour force survey 2015* <http://bit.ly/1RybHWs> (accessed 25 June 2015). See also Cosatu *Statement* <http://bit.ly/1LyErgi> (accessed 23 June 2015).

⁴⁹ WB *Unemployment, total (% of total labour force) (modelled ILO estimate)* <http://bit.ly/1ojrRV9> (accessed 25 June 2015).

⁵⁰ STATS SA *General household survey 2014* <http://bit.ly/1Ndl2kk> (accessed 25 June 2015).

⁵¹ Hereafter the 'SARS'.

⁵² See also National Treasury and the SARS *2014 Tax Statistics* <http://bit.ly/1CDON8I> (accessed 25 June 2015).

individual tax may be the number of taxpayers assessed which is set at 5.2 million for the 2013 financial year – roughly representing 10% of the population.⁵³

According to the World Bank, South Africans are the most indebted individuals in the world.⁵⁴ However, what is more concerning is the extent to which such indebtedness has developed into over-indebtedness which is evident from credit bureau reports. At the end of December 2014 credit bureaux had records of 22.84 million credit active consumers, of which 10.26 million had impaired credit records. Thus, only 55% of credit-active consumers were in ‘good standing’⁵⁵ which is a clear indication that South African natural person consumers are heavily over-indebted.⁵⁶ This is despite the fact that it is generally accepted that the NCA, which became fully effective on 1 June 2007,⁵⁷ shielded South Africa to some extent from the worst of the 2007/2008 worldwide economic meltdown.⁵⁸ Although its stringent measures to prevent reckless credit granting⁵⁹ and over-indebtedness were implemented at an opportune time, the NCA ostensibly has little to offer once over-indebtedness has set in, as can be deduced from the earlier preliminary discussion of the debt review procedure and which will further be discussed below.⁶⁰

If a South African debtor fails to pay his debt, a creditor will eventually obtain judgment (in most instances default judgment) against the defaulting debtor.⁶¹ It is important to note that no natural person is protected from debt enforcement procedures prior to the invocation of one of the three statutory debt relief measures.⁶² Once a creditor has obtained a judgment it will only prescribe once a

⁵³ *Ibid.*

⁵⁴ WB *Global index database* <http://bit.ly/1zpsu5J> (accessed 23 June 2015) and Moneyweb *South Africans are the world’s biggest borrowers* <http://bit.ly/1RxxTS0> (accessed 23 June 2015).

⁵⁵ ‘Good standing’ refers to ‘[a]n account or consumer showing as current or on which the client has not missed more than one or two instalments, which has no adverse listings and has no judgments’: NCR *Credit bureaux monitor* <http://bit.ly/1SFL2JM> (accessed 23 June 2015).

⁵⁶ *Ibid.*

⁵⁷ Proc 22 in GG 28824 of 11 May 2006.

⁵⁸ See Woker 2010 *Obiter* 231.

⁵⁹ See ch 5 par 5.5 on the NCA’s reckless credit provisions.

⁶⁰ See further the discussions in ch 4 par 4.3 and ch 5 para 5.4 and 5.5.

⁶¹ In most cases judgment will be obtained from the magistrates’ courts. These are the lower courts which function within the framework of the Magistrates’ Courts Act.

⁶² See ch 3 par 3.3 and ch 4 para 4.2 and 4.3.

period of 30 years has lapsed.⁶³ Where the debt was secured, the credit provider will be entitled to call on his security. If the debt is not secured and the debtor has assets that can be sold in execution, the judgment creditor may decide on such a sale. Another possibility is the attachment of emoluments. In this regard salaries or wages are generally attached by making use of an emoluments attachment order, an effective and widely used method to collect on judgment debt where the debtor is employed in the formal sector.⁶⁴ In terms of such an order, an employer is obliged to deduct instalments from the debtor's salary or wage and pay these amounts over to the creditor. Although there is nothing sinister about the existence of such a measure, some of its features may result in untenable situations: for example, there is no statutory prescription as to the percentage of the salary or wage that may be attached. Furthermore, neither the credit provider nor the clerk of the court granting the order is necessarily aware of other emoluments attachment orders already made against the debtor's salary or wage. There is generally no inquiry into the financial affairs of the debtor and the creditor often unilaterally decides on the amount of the instalment. If a substantial part (or the whole – which is not a rare occurrence) of a debtor's salary or wage is attached in this manner, it leaves him with no means to provide for himself and his dependants. Due to the lack of protection, the debtor is in such instances forced to resign⁶⁵ and to seek employment in the informal sector.⁶⁶ If these debtors cannot find a source of income in the informal sector, they become a social burden on the South African economy. Even where a South African debtor does not have sufficient attachable assets or income, which will make it very difficult to collect on his debt, he may technically be the subject of harassment for a period of

⁶³ This statement is concerned with extinctive prescription; Prescription Act 68 of 1969, s 11. The Act applies to debts arising after 1 December 1970. There are two forms of prescription, namely, extinctive and acquisitive prescription. Extinctive prescription refers to the situation where legal obligations are extinguished through lapse of time whilst acquisitive prescription refers to the situation where ownership of another's property can be acquired once a period of 30 years have lapsed. See Otto and Prozesky-Kuschke 'Breach of contract and termination of contractual relationship' 151. See further ch 5 par 5.8.

⁶⁴ Magistrates' Courts Act, s 65J. See in general University of Pretoria Law Clinic *Garnishee orders and A follow up report*. The University of Stellenbosch Legal Aid Clinic will in all probability challenge the constitutionality of certain aspects relating to the emoluments attachment order procedure in the Constitutional Court in 2015.

⁶⁵ See Pitman 'A multi-pronged attack' 152.

⁶⁶ The informal sector refers to the unstructured economy in developing countries where individuals are not formally employed, but are engaged in entrepreneurial activities which do not adhere to legal requirements, standards and procedures. These individuals refrain from entering the formal economy as once they do so, their wages will again be attached. These entrepreneurs include street vendors, hairdressers, musicians, artisans, etc.

at least 30 years in which prescription runs. Therefore, some aspects of the individual enforcement system coupled with the exclusivity of the broader insolvency regime entrench the reality of the dual South African economy. This is so since the system, through its apparent lack of remedial measures, in some instances retains these 'poor' South Africans in a state of poverty or even worse, forces individuals forming part of the formal economy to enter the secondary economy which may result in them becoming NINA debtors.⁶⁷ In this regard, the following comment by Spooner, describing how individual insolvency laws could provide a solution in this respect, is very appropriate:⁶⁸

Debt discharge allows personal insolvency law to alleviate poverty and deprivation among the inevitable financially failed households and safeguard the basic needs of all society members, while removing households from financial exclusion by providing a fresh start.

In my search for a solution to the debt problems associated with those South African natural person debtors who do not have any form of recourse available, I have come to realise that the need for law reform has been recognised by academics and to a lesser extent the legislature, but that government has not made any concrete effort to rise to the occasion.⁶⁹ This thesis therefore, amongst others, attempts to motivate the need for a total reappraisal of the system from a debt relief perspective. Such motivation will be put forward by, amongst others, conducting a proper evaluation of the system in light of the right to equality as entrenched in the South African Constitution.⁷⁰ I take this route as it has not been properly considered thus far even though a finding that the system is in contravention of the Constitution may cause the matter to gain momentum. In this regard, Evans first raised the issue of the

⁶⁷ Coetzee and Roestoff 2013 *Int Insolv Rev* 192.

⁶⁸ Spooner *Personal insolvency law* 74. This research is unpublished and cited with the author's permission.

⁶⁹ See discussions above.

⁷⁰ The Constitution of the Republic of South Africa of 1996 (hereafter the 'Constitution'). See Fletcher *The law of insolvency* vii where he already in 2002 raised the issue, within the context of England and Wales, of human rights and more specifically the Human Rights Act 1998 that necessitates a review of the operation of insolvency and procedure. He warns that the validity of established provisions will be challenged in court with increasing frequency. Fletcher also (at 24) refers to the fact that the rights of natural person insolvents may be affected by human rights treaties. See further Fletcher *The law of insolvency* 27 where these sentiments were repeated in 2009.

possible unconstitutionality of the demonstrated differentiation that occurs in South African natural person insolvency law in the following terms:⁷¹

Although the [Insolvency] Act does not provide for different classes of debtors who are to be treated differently in accordance with differing or changing circumstances, it does in fact differentiate between those 'rich debtors' who are able to prove advantage to creditors, and the 'poor debtors' who cannot. This raises the question whether, under present legislation, the door has been opened for these 'poor debtors' to question the constitutionality of their position.

Although Evans's question was raised within the narrow context of the sequestration order as a debt relief measure *per se* it is even more pertinent within the context of the broader South African natural person insolvency law, which includes the secondary debt relief measures. The quoted passage and the stated question therefore serve as significant indicators of the relevance of this thesis and the small acorn that evolved into the discussions below.⁷²

As regards its debt relief measures, the South African insolvency system should be measured against the right to equality which is entrenched in both the Constitution and the Promotion of Equality and Prevention of Unfair Discrimination Act.⁷³ This right must be explored by referring to both Acts as different procedures and remedies are involved. The Equality Act has added to the understanding of the constitutional right to equality. The constitutional framework is discussed first, whereafter the Equality Act's structure is set out. The basic law and some arguments are put forward in this chapter. However, the actual tests, where the different statutory debt relief procedures and their consequences are measured against the law set out in this chapter, are only conducted in subsequent chapters.⁷⁴

Chapter 2 of the Constitution contains the Bill of Rights⁷⁵ which forms the cornerstone of our democracy. The Bill protects the rights of all people in the country and confirms the democratic values of human dignity, equality and freedom.⁷⁶ The

⁷¹ Evans 2002 *Int Insolv Rev* 34. See also Steyn 2004 *Int Insolv Rev* 11; Boraine and Roestoff 2014 *THRHR* 374 and Boraine and Evans 'The law of insolvency and the Bill of Rights' 4A8.

⁷² See below as well as ch 3 par 3.5 and ch 4 par 4.4.

⁷³ 4 of 2000 (hereafter the 'Equality Act').

⁷⁴ Ch 3 par 3.5 and ch 4 par 4.4.

⁷⁵ Hereafter the 'Bill'.

⁷⁶ S 7(1).

state has the express duty to respect, protect, promote and fulfil the rights set out in chapter 2.⁷⁷ However, such rights are not absolute and are subject to limitations contained or referred to in section 36 or elsewhere in the Bill.⁷⁸

Section 8, which deals with the application of the Bill, provides that the latter applies to all law and binds all spheres of government, namely, the legislature, executive and judiciary. It further binds all organs of state.⁷⁹ Natural and juristic persons are bound to the Bill's provisions if and to the extent applicable with reference to the nature of the right and the duty that it imposes.⁸⁰

Section 36 is titled 'limitation of rights' and provides that the rights in the Bill may only be limited in terms of law of general application to the extent that it is reasonable and justifiable to do so in an open and democratic society based on human dignity, equality and freedom. In such an instance, all relevant factors should be taken into account, which include:⁸¹

- (a) the nature of the right;
- (b) the importance of the purpose of the limitation;
- (c) the nature and extent of the limitation;
- (d) the relation between the limitation and its purpose; and
- (e) less restrictive means to achieve the purpose.

No law may limit a right embedded in the Bill except as provided for in section 36 or elsewhere in the Constitution.⁸²

It is clear that the equality principle is one of three democratic values that take centre stage in the Bill.⁸³ The right to equality is the first right in the Bill and is provided for in section 9⁸⁴ as follows:

- (1) Everyone is equal before the law and has the right to equal protection and benefit of the law.

⁷⁷ S 7(2).

⁷⁸ S 7(3).

⁷⁹ S 8(1).

⁸⁰ S 8(2).

⁸¹ S 36(1).

⁸² S 36(2).

⁸³ S 7(1) and s 36(1).

⁸⁴ See in general Albery and Goldblatt 'Equality' ch 35 and Currie and De Waal *Bill of Rights* ch 9 for discussions of the right to equality.

- (2) Equality includes the full and equal enjoyment of all rights and freedoms. To promote the achievement of equality legislative and other measures designed to protect or advance persons, or categories of persons, disadvantaged by unfair discrimination may be taken.
- (3) The state may not unfairly discriminate directly or indirectly against anyone on one or more grounds, including race, gender, sex, pregnancy, marital status, ethnic or social origin, colour, sexual orientation, age, disability, religion, conscience, belief, culture, language and birth.
- (4) No person may unfairly discriminate directly or indirectly against anyone on one or more grounds in terms of subsection (3). National legislation must be enacted to prevent or prohibit unfair discrimination.
- (5) Discrimination on one or more of the grounds listed in subsection (3) is unfair unless it is established that the discrimination is fair.

The equality concept is said to be a difficult and deeply controversial social ideal. In its most fundamental and abstract form, the idea is that those who are similarly situated should be similarly treated. Consequently, those who are not similarly situated should be treated dissimilarly.⁸⁵ Currie and De Waal argue that it is not the idea of equality that is so challenging, but two ancillary issues thereto, namely, what is relevant in determining the similarities in people's situations and secondly, what constitutes equal treatment of those similarly situated.⁸⁶ Within the ambit of natural person insolvency law it can be argued that all insolvent natural persons universally face the exact same difficulties, namely, the inability to service debt and the consequential socio-economic adversities attached thereto. What is dissimilar to individuals' debt-related predicaments is the level of contribution that these individuals can make towards servicing part of their debt. Therefore, it needs to be established whether debtors facing the same financial predicament, but without the same level of repayment capacity, should be treated equally, and if so, what constitutes equal treatment within the context of insolvency law.

Currie and De Waal also note that although South Africa's inequality problems are mainly attributed to historical discrimination on the basis of race, it can no longer be explained by reference to race alone as class is emerging as an indicator of inequality.⁸⁷ This notion is especially relevant in the context of natural person insolvency law and even more specifically with regard to NINA debtors who typically

⁸⁵ Currie and De Waal *Bill of Rights* 210.

⁸⁶ *Idem* 210–211.

⁸⁷ *Idem* 212.

form part of South Africa's 'secondary economy' and who are presently excluded from any statutory debt relief procedure as was illustrated earlier in the discussion.⁸⁸ In this regard the right to equality, which is a powerful commitment to the transformation of society, and particularly to achieve substantive equality which can according to Albertyn *et al* be explained as equality in social and economic life,⁸⁹ should be considered as a possible avenue in reaching a solution to the plight of especially NINA debtors. Substantive equality recognises that inequality is not only the cause of the different treatment of persons, but more often emerges from 'systemic group based inequalities that shape relations of dominance and subordination, and material disparities between groups'.⁹⁰ It is therefore important to oppose substantive inequality, ensuring equality of outcome, as opposed to mere formal inequality.⁹¹ This need is recognised particularly in section 9(2) of the Constitution which refers to measures 'designed to protect or advance persons, or categories of persons disadvantaged by unfair discrimination'. In this regard substantive equality considers the social and economic conditions of groups or individuals to ensure that constitutional equality is realised. Results or effects as opposed to mere form are emphasised.⁹²

In *Harksen v Lane*,⁹³ which was decided under the Interim Constitution,⁹⁴ the Constitutional Court set out three distinct steps of an investigation into an alleged violation of the right to equality. The stages of enquiry are as follows:⁹⁵

- (a) Does the provision differentiate between people or categories of people? If so, does the differentiation bear a rational connection to a legitimate government purpose? If it does not then there is a violation of s 8(1).⁹⁶ Even if it does bear a rational connection, it might nevertheless amount to discrimination.

⁸⁸ See also Coetzee and Roestoff 2013 *Int Insolv Rev* pt 2.

⁸⁹ See Albertyn *et al Introduction* 1.

⁹⁰ *Ibid.*

⁹¹ See *President of the Republic of South Africa v Hugo* 1997 (4) SA 1 (CC) 23.

⁹² Currie and De Waal *Bill of Rights* 213.

⁹³ 1998 (1) SA 300 (CC). See Freedman 1998 *SALJ* 243 and Rautenbach 1998 *TSAR* 329 for discussions of the case.

⁹⁴ Constitution of the Republic of South Africa 200 of 1993 (hereafter 'Interim Constitution'). The relevant provisions of the Interim Constitution are analogous to provisions in the Constitution and therefore *Harksen v Lane* remains the *locus classicus* as far as the determination of unfair discrimination is concerned.

⁹⁵ *Harksen v Lane* 324–325.

⁹⁶ S 8(1) of the Interim Constitution is similar to s 9(1) of the Constitution.

- (b) Does the differentiation amount to unfair discrimination? This requires a two-stage analysis:
- (i) Firstly, does the differentiation amount to 'discrimination'? If it is on a specified ground, then discrimination will have been established. If it is not on a specified ground, then whether or not there is discrimination will depend upon whether, objectively, the ground is based on attributes and characteristics which have the potential to impair the fundamental human dignity of persons as human beings or to affect them adversely in a comparably serious manner.
 - (ii) If the differentiation amounts to 'discrimination', does it amount to 'unfair discrimination'? If it has been found to have been on a specified ground, then unfairness will be presumed. If on an unspecified ground, unfairness will have to be established by the complainant. The test of unfairness focuses primarily on the impact of the discrimination on the complainant and others in his or her situation.
- If, at the end of this stage of the enquiry, the differentiation is found not to be unfair, then there will be no violation of s 8(2).⁹⁷
- (c) If the discrimination is found to be unfair then a determination will have to be made as to whether the provision can be justified under the limitations clause.⁹⁸

Applying the above test to the limited access to South African debt relief measures, it is safe to say that the broader natural person insolvency system at the very least differentiates between categories of people, by amongst others drawing a distinction between those who have something to offer creditors, be it assets or income, and those who do not have something to offer.⁹⁹ This is so since the 'haves' are allowed access to the system, through one of the three statutory debt relief measures, but the 'have nots' are excluded from any form of statutory recourse. One could possibly argue that this distinction qualifies as discrimination based on the listed ground of 'social origin' which according to *Albertyn et al* encompasses 'class' and can be used to address unfair discrimination based on socio-economic status.¹⁰⁰ If the exclusion does resort under this ground, discrimination will be established and unfairness

⁹⁷ S 8(2) of the Interim Constitution is similar to s 9(3) of the Constitution.

⁹⁸ The Interim Constitution's limitations clause can be found in s 33. As was already noted s 36 of the Constitution contains its limitations clause.

⁹⁹ The term 'differentiation' is used when a distinction is made on an unlisted ground. See *Pretoria City Council v Walker* 1998 (2) SA 363 (CC) 380 and *Harksen v Lane* 321. See also Kok 2011 *THRHR* 242–244.

¹⁰⁰ *Albertyn et al Introduction* 79–80. They argue that the ground refers to one's social group or social status. Class, family and clan membership can all be subsumed under the meaning of social origin. To the extent that social origin can be equated with class, this ground could be used to address unfair discrimination arising from one's low socio-economic status.

presumed, which will shift the onus to the respondent. However, the meaning of 'social origin' has not been judicially determined as yet and therefore the more conservative route should rather be followed by not idly accepting that socio-economic status in the present context (or at all) necessarily resorts under 'social origin'. On another level, the system differentiates or discriminates (if one accepts that socio-economic status resorts under the listed ground of 'social origin') by only offering a discharge of debt to those who qualify for the sequestration procedure specifically. This is so since individuals with sufficient assets qualify for sequestration and the consequential discharge as opposed to those with disposable income, but insufficient assets to show that the liquidation of their estates would result in a benefit for creditors. The latter debtors may qualify for secondary statutory debt relief measures, but will not receive a discharge. NINA debtors are obviously also affected by the fact that only the sequestration procedure offers a discharge as they do not have access to any measure at present, let alone the sequestration procedure. As regards the NINA category of debtors a further argument can be made that their exclusion amounts to indirect unfair discrimination on the listed ground of 'race' as it is an undisputed fact that proportionately more black South Africans can be categorised as NINA debtors than white South Africans. Even though South African insolvency law seems neutral as regards race, its effect is that mostly black individuals are excluded.¹⁰¹ However, as is the case with 'social origin', this thesis sets out on the more cautious route by measuring the differentiation that occurs in natural person insolvency against the complete *Harksen v Lane* test.

If one accepts that differentiation does occur, it has to be determined whether it bears a rational connection to a legitimate government purpose.¹⁰² However, even if it does bear such a connection it may still amount to discrimination. Unfair discrimination¹⁰³ was defined in *Prinsloo v Van der Linde* as 'treating persons

¹⁰¹ See *Pretoria City Council v Walker* 363 for an example of indirect discrimination on a racial basis.

¹⁰² See *Prinsloo v Van der Linde* 1997 (3) SA 1012 (CC) 1024 for an example of differentiation that did not amount to unfair discrimination and consequently came down to 'mere differentiation'.

¹⁰³ See *President of the Republic of South Africa v Hugo* for an example of fair discrimination. This case was the result of a special remission of sentences that the late former president Mandela granted to certain categories of prisoners in terms of Presidential Act 17 of 1994. One category was all mothers in prison with children under the age of twelve years. The respondent alleged that the Presidential Act was in violation of s 8(1) and (2) of the interim Constitution as it unfairly discriminated against him (the father of a child under the age of twelve years) on grounds of sex

Footnote continues on next page

differently in a way which impairs their fundamental dignity as human beings, who are inherently equal in dignity'.¹⁰⁴ As was mentioned, if it is accepted that socio-economic status resorts under 'social origin', discrimination is established and unfairness is presumed. The same reasoning applies to 'race'. Otherwise, if the differentiation does not resort under 'social origin' or 'race', discrimination and unfairness must be determined. The test for discrimination and unfairness can be deducted from the quote from *Harksen v Lane* above. As regards the latter, various factors must be considered, including¹⁰⁵

- (a) the position of the complainants in society and whether they have suffered in the past from patterns of disadvantage, whether the discrimination in the case under consideration is on a specified ground or not;
- (b) the nature of the provision or power and the purpose sought to be achieved by it;
- (c) with due regard to (a) and (b) above, and any other relevant factors, the extent to which the discrimination has affected the rights or interests of complainants and whether it has led to an impairment of their fundamental human dignity or constitutes an impairment of a comparably serious nature.

The final step in a constitutional enquiry is to ascertain whether established unfair discrimination can be justified under the limitations clause. However, it is unclear how discrimination that has been categorised as being 'unfair', as it has attributes and characteristics which can potentially impair the human dignity of people as human beings, could ever be acceptable in an open and democratic society based on human dignity, freedom and equality. Nevertheless, the Constitutional Court does apply section 36 in matters where an infringement of the right to equality is alleged,

or gender and indirectly against his son in terms of s 8(2) as his parent was not a female. It was stated in the judgment (at 26) that

it cannot be said, for example, that the effect of the discrimination was to deny or limit their [fathers'] freedom, for their freedom was curtailed as a result of their conviction, not as a result of the Presidential Act. That Act merely deprived them of an early release to which they had no legal entitlement.

The same reasoning may apply in the context of insolvency law and specifically relating to the discharge of debt in terms of the sequestration procedure, namely, that it is not the Insolvency Act that deprives excluded natural persons from an early discharge of debt, but their incurrence of excessive credit or at the very least their insolvency. However, in *President of the Republic of South Africa v Hugo* vulnerable groups received an advantage over less-vulnerable groups whereas in insolvency law, in South Africa, a less-vulnerable group receives an advantage over generally more vulnerable groups.

¹⁰⁴ *Prinsloo v Van der Linde* 1026.

¹⁰⁵ *Harksen v Lane* 324.

although its application has not led to any of the challenged laws being upheld thus far.¹⁰⁶

In concluding the initial constitutional enquiry, it seems that a significant probability exists that the broader insolvency system would fail a constitutional challenge – a serious allegation in need of further analysis. What has already been established is that the natural person insolvency system at the very least differentiates between categories of persons. What must further be determined, in accordance with the parameters set out above, is whether such differentiation results in unfair discrimination, and if so, whether it is justifiable.

It is interesting to note that the Belgian Constitutional Court in April 2003¹⁰⁷ held that the exclusion of debtors who are unable to pay a substantial portion of their debt from the opportunity to benefit from a legal settlement plan violates the Belgian Constitution. Insufficient income was therefore held not to be a justifiable ground to refuse a plan that would discharge all pre-petition debt.¹⁰⁸

As far as the Equality Act¹⁰⁹ is concerned, it is important to emphasise that the Act is not detached from the Constitution as it was promulgated in line with section 9(4) and item 23 of schedule 6¹¹⁰ thereof.¹¹¹ It became wholly effective on 16 June 2003.¹¹² The majority of cases dealing with the right to equality must, after commencement of the Equality Act, be dealt with in terms of its provisions as opposed to a direct constitutional challenge in terms of section 9 of the Constitution.¹¹³ Only where a challenge falls beyond the reach of the Equality Act,

¹⁰⁶ Currie and De Waal *Bill of Rights* 218 and authorities cited in n38.

¹⁰⁷ Order No 3/2003 (3 April 2003) <http://bit.ly/1Lug83Y> (accessed 16 December 2014). See Kilborn 2006 *Am Bankr Inst L Rev* 94; Kilborn 'Inaugural lecture' 2010 33 <http://bit.ly/1BoDJAP> (accessed 28 February 2015); and Spooner 2013 *ERPL* 755.

¹⁰⁸ *Ibid.*

¹⁰⁹ See in general Albertyn *et al Introduction*; Albertyn and Goldblatt 'Equality' par 35.8 and Currie and De Waal *Bill of Rights* par 9.6 on the Equality Act.

¹¹⁰ This item deals with the transitional arrangements relating to the Bill.

¹¹¹ See the long title as well as the preamble to the Equality Act.

¹¹² Proc No 49 GG No 25065 of 13 June 2003.

¹¹³ 'Equality' is defined in s 1(1) of the Equality Act. It provides that the concept includes the full and equal enjoyment of rights and freedoms as contemplated in the Constitution and includes *de jure* and *de facto* equality and also equality in terms of outcome.

may the constitutional right to equality be relied upon.¹¹⁴ However, the Equality Act gives effect to the right to equality as entrenched in the Constitution¹¹⁵ and can therefore not reduce constitutional protection, although it can be increased.¹¹⁶ The Equality Act is therefore likely to be interpreted as providing the same protection as the constitutional right to equality and jurisprudence interpreting section 9 of the Constitution will continue to play a central role.¹¹⁷ The Equality Act has unfortunately rarely been used and therefore very few cases have been reported in terms of its provisions.¹¹⁸

The following extracts from the Act's preamble are particularly important in the context of this thesis:¹¹⁹

The consolidation of democracy in our country requires the eradication of *social and economic inequalities*, especially those that are *systemic in nature*, which were generated in our history by colonialism, apartheid and patriarchy, and which brought pain and suffering to the great majority of our people;

Although significant progress has been made in restructuring and transforming our society and its institutions, *systemic inequalities* and unfair discrimination remain deeply embedded in social structures, practices and attitudes, undermining the aspirations of our constitutional democracy.

By quoting the above extracts, I do not necessarily argue that the inequality brought about by the broader insolvency laws is the product of colonialism, apartheid and/or patriarchy. However, one cannot escape the fact that the Equality Act strives to eradicate systemic social and economic inequalities. Section 6 takes centre stage and provides that '[n]either the State nor any person may unfairly discriminate against any person'.¹²⁰

Two definitions, that of 'discrimination' and 'prohibited grounds' are important. The Equality Act provides that 'discrimination'

means any act or omission, including a policy, *law*, rule, practice, condition or situation which directly or indirectly-

¹¹⁴ See Currie and De Waal *Bill of Rights* 245.

¹¹⁵ See s 3(1)(a).

¹¹⁶ See in general Kok *A socio-legal analysis* 141.

¹¹⁷ *Idem* 245.

¹¹⁸ See Albertyn and Goldblatt 'Equality' par 35.8 and cases cited there.

¹¹⁹ My emphasis.

¹²⁰ 'Person' is defined in s 1(1) as including 'a group or category of persons'.

- (a) imposes burdens, obligations or disadvantage on; or
- (b) withholds benefits, opportunities or advantages from, any person on one or more of the prohibited grounds.¹²¹

'Prohibited grounds' are defined as

- (a) race, gender, sex, pregnancy, marital status, ethnic or social origin, colour, sexual orientation, age, disability, religion, conscience, belief, culture, language and birth; or
- (b) any other ground where discrimination based on that other ground-
 - (i) causes or perpetuates *systemic disadvantage*;
 - (ii) undermines human dignity; or
 - (iii) adversely affects the equal enjoyment of a person's rights and freedoms in a serious manner that is comparable to discrimination on a ground in paragraph (a).¹²²

Although the Equality Bill specifically included HIV/AIDS, socio-economic status, nationality, family responsibility and family status as grounds under paragraph (a) of the definition of prohibited grounds, Cabinet decided to remove them. It was decided to include a directive in section 34 instead which provides that:

- (1) In view of the overwhelming evidence of the importance, impact on society and link to systemic disadvantage and discrimination on the grounds of HIV/AIDS status, socio-economic status, nationality, family responsibility and family status-
 - (a) special consideration must be given to the inclusion of these grounds in paragraph (a) of the definition of "prohibited grounds" by the Minister;
 - (b) the Equality Review Committee must, within one year, investigate and make the necessary recommendations to the Minister.
- (2) Nothing in this section-
 - (a) affects the ordinary jurisdiction of the courts to determine disputes that may be resolved by the application of law on these grounds;
 - (b) prevents a complainant from instituting proceedings on any of these grounds in a court of law;
 - (c) prevents a court from making a determination that any of these grounds are grounds in terms of paragraph (b) of the definition of "prohibited grounds" or are included within one or more of the grounds listed in paragraph (a) of the definition of "prohibited grounds".

Unfortunately, for purposes of the present discussion, socio-economic status was not included in paragraph (a) of the definition of prohibited grounds as is evident from the quoted definition. Nevertheless, what is significant is that the legislature regards

¹²¹ S 1(1). My emphasis.

¹²² *Ibid.*

socio-economic status as an important ground to consider. The concept is defined in section 1(1) as including

a social and economic condition or perceived condition of a person who is disadvantaged by poverty, low employment status or lack of or low-level educational qualifications.

Albertyn *et al* note that socio-economic status refers, amongst others, to income, employment and education levels. They submit that it is similar but not identical to class as it is inclined to determine political and economic power. Although they are also in favour of the inclusion of the ground in paragraph (a) of the definition of prohibited grounds, their suggestion has clearly not been followed thus far. As noted in the constitutional discussion, the authors are of the opinion that the concept overlaps with social origin. It may further overlap with race and gender which are also included as listed prohibited grounds.¹²³

Considering the above, it is clear that the illustrated systemic exclusions resulting from the natural person insolvency system are effected in terms of socio-economic status as defined in the Equality Act. This is so as NINA debtors especially are excluded from remedial measures. Furthermore, as was referred to in the discussion with regard to the Constitution, it can be argued that the distinctions drawn by the insolvency system probably resonate under the listed ground of 'social origin'. Unfortunately this concept has also not been defined in the Equality Act or judgements in terms thereof. 'Socio-economic status' may further overlap with 'race' in the present context as the proportionate majority of insolvent debtors are black. It may therefore be found that, in terms of the Equality Act, the broader insolvency system discriminates, albeit indirectly, on a racial basis. Section 7 of the Equality Act lists some forms of discrimination on racial grounds. Section 7(e) is important as it provides that

[s]ubject to section 6, no person may unfairly discriminate against any person on the ground of race, including-

(e) the denial of access to opportunities, including access to services or contractual opportunities for rendering services for consideration, or failing to take steps to reasonably accommodate the needs of such persons.

¹²³ Albertyn *Introduction* 84–85.

However, as was mentioned, the distinctions that the larger insolvency system draws on the basis of socio-economic status are conservatively treated as not necessarily resorting under 'social origin' (and/or 'race') even though it may very well be the case. The more involved route must also be followed here to show that, within the context of natural person insolvency law, 'socio-economic status' resorts under paragraph (b) of the definition of prohibited grounds.

In order to prove that the insolvency system unfairly discriminates against a group of debtors in terms of the Equality Act, certain procedural matters are of relevance. Fortunately, the legislature has in this regard eased the task of the plaintiff or applicant that usually carries the heaviest burden of proof in civil litigation.¹²⁴ This is so since section 13¹²⁵ shifts the burden of proof to the respondent once a *prima facie* case of discrimination has been made out.¹²⁶ Another advantage is that unfair discrimination is not only presumed on a prohibited ground, as is the case in terms of a constitutional challenge, but also on similar grounds.¹²⁷ The respondent must therefore take cognisance of section 14 which is titled 'Determination of fairness or unfairness'.¹²⁸ Section 14(2) provides that three matters should be taken into account when determining whether discrimination is fair. These are context; factors as set out in subsection (3); and 'whether the discrimination reasonably and justifiably differentiates between persons according to objectively determinable criteria, intrinsic to the activity concerned'. The factors listed in subsection (3) are as follows:

- (a) Whether the discrimination impairs or is likely to impair human dignity;
- (b) the impact or likely impact of the discrimination on the complainant;

¹²⁴ See Kok *A socio-legal analysis* 136 *et seq.*

¹²⁵ Currie and De Waal *Bill of Rights* 246 n185 argue that s 13 is not applicable to challenges to the validity of law and that a conflict between the Equality Act and other laws should be dealt with in terms of s 5(2). However, it seems that the broader natural person insolvency scheme infringes the right to equality as opposed to specific legislative provisions. I am not convinced that s 13 has no application to South African natural person insolvency law. S 5(2) of the Equality Act provides as follows:

If any conflict relating to a matter dealt with in this Act arises between this Act and the provisions of any other law, other than the Constitution or an Act of Parliament expressly amending this Act, the provisions of this Act must prevail.

¹²⁶ S 13(1).

¹²⁷ S 13(2) read together with the definition of prohibited grounds in s 1.

¹²⁸ See Kok *A socio-legal analysis* 146 *et seq.* for a discussion of s 14.

- (c) the position of the complainant in society and whether he or she suffers from patterns of disadvantage or belongs to a group that suffers from such patterns of disadvantage;
- (d) the nature and extent of the discrimination;
- (e) whether the discrimination is systemic in nature;
- (f) whether the discrimination has a legitimate purpose;
- (g) whether and to what extent the discrimination achieves its purpose;
- (h) whether there are less restrictive and less disadvantageous means to achieve the purpose;
- (i) whether and to what extent the respondent has taken such steps as being reasonable in the circumstances to-
 - (i) address the disadvantage which arises from or is related to one or more of the prohibited grounds; or
 - (ii) accommodate diversity.

Unlike the Constitution, the Equality Act does not contain a limitations clause which can be used by the respondent to argue that unfair discrimination is justifiable.

In employing the standards of the Equality Act it is evident that the differentiation that the natural person insolvency system brings about takes place by means of law which directly and indirectly withholds benefits, opportunities and advantages from those who are excluded from statutory debt relief measures on the basis of their socio economic status.¹²⁹ Within the present context, socio-economic status could at least resort under paragraph (b) of the definition of prohibited grounds. Secondly, even those who do qualify for secondary debt relief measures may be discriminated against on socio-economic grounds as 'assetless' insolvents do not enjoy the privilege of a discharge. Those who qualify for secondary debt relief measures and who have sufficient income to service their debt obligations over a slightly longer period will not be able to show that they are, on the basis of socio-economic grounds, discriminated against, as can be deduced from its definition. However, those who have some disposable income available and who are subject to secondary debt relief measures, but who face excessively long repayment terms (or who may in some instances be subject to such procedures indefinitely) due to low income and low employment could possibly succeed in arguing discrimination along the same lines as the NINA debtors. If such a case of discrimination is made out, the burden of proof will shift to the respondent in terms of section 13. Even though the

¹²⁹ In accordance with the definition of discrimination in s 1(1).

unfairness of the discrimination will be presumed it must still in terms of section 14 be determined in disputed cases.

The discussion of the right to equality in terms of the Constitution and the Equality Act shows that it is possible that the broader natural person insolvency system is probably in contravention of this right and an urgent investigation is therefore appropriate. Should such an investigation reveal that this is in fact the case, it would serve as a powerful tool to spur reform.

Spooner's observation regarding the possibility of reform is appropriate here:

Universal political forces, rather than inherently national factors, represent greater obstacles to reforming personal insolvency law to meet the needs of the modern consumer credit society.¹³⁰

He cautions commentators and policymakers to not hastily assume that a country's personal insolvency system is in all instances the expected product of distinctly national factors.¹³¹ According to him, natural person insolvency laws are the outcome of complex political conflicts and compromises.¹³² In this regard he mentions universal ideological conflicts; public opinion and policy salience; interest group influence;¹³³ and the interplay of ideology, public opinion and interest groups as factors.¹³⁴ Given these political difficulties in reforming insolvency law, he argues that perceptions that reform would be contrary to national legal traditions, structural features and cultural attitudes should be avoided. This is so since anti-reform arguments based on these 'nation-centric' arguments may be used to further political ideology or interest group preferences which will suppress beneficial reform. In this

¹³⁰ Spooner 2013 *ERPL* 747. See also Spooner 2012 *Am Bankr LJ* 243 in general.

¹³¹ Spooner 2013 *ERPL* 788.

¹³² See also Niemi 2012 *J Consum Policy* 458 who states that 'over-indebtedness is a politically and ethically sensitive issue'.

¹³³ Spooner 2013 *ERPL* 774–784. See also Ramsay 2012 *J Consum Policy* 429 who explains that the

extent of debt relief in a country depends on the effectiveness of spokespersons such as consumer or social welfare groups, lawyers or counselling professionals who may be able to harness the media through the use of dramatic stories to create a political demand for action.

Ramsay 425 also refers to the social construction of debtors and notes that

[i]mages of debtors and creditors are central to the politics of reform and interest groups promote differing conceptions of debtors and creditors. Social science research is closely linked therefore to politics and policy making.

¹³⁴ Spooner 2013 *ERPL* 784–786. Ramsay 2012 *J Consum Policy* 427 mentions that differences in institutional approaches to individual insolvency 'may reflect the political economy of interest groups, ideology or simply a form of institutional path dependency'.

manner 'foreign' international best practice is discarded and reform is postponed until mass insolvency calamities materialise. Spooner suggests that societies should rather adopt *ex ante* regulatory measures and that as much learning as possible should be drawn from international experiences to prevent the painful wait for relief whilst legislation is being reformed in times of crisis. He does not call for legal transplants, but strongly argues that national factors should not be over-emphasised.

When contemplating the development of national consumer insolvency laws (or the lack thereof) in South Africa, the 'social dynamite'¹³⁵ that debt represents may explain the slow pace at which reform is taking place. This is so since the universal differences in political ideology are extremely pertinent in South Africa as a result of its dual economy and the ever increasing gap between classes. Furthermore, public opinion has not had a major impact on insolvency law reform due to the low salience of the matter in the larger society's consciousness. This is so despite the apparent lack of effective debt relief measures. One explanation for the public's ignorance of the matter might be the focus on poverty *per se* without always realising its important link with over-indebtedness. At most public opinion has, in the broader context of over-indebtedness, influenced policy as regards adverse information held by credit bureaux and reckless credit extension which has in both instances led to actual intervention.¹³⁶ Another possibility for the lack of mobilisation might be the public's indoctrination with 'absolute' concepts such as the sanctity of contracts, which are accepted as canon law.¹³⁷ The possibility that these 'entrenched concepts' may be used as instruments to oppress classes of debtors, and especially the poor, has not (as yet) entered the larger public's consciousness. Further, as Spooner explains,¹³⁸ policy salience brings matters to policymakers' agendas, whereas interest group

¹³⁵ Sullivan *et al* *As we forgive* 334.

¹³⁶ See the removal of adverse consumer credit information and information relating to paid up judgments regulations GN R144 in GG 37386 of 26 February 2014 and the discussion of reckless credit provisions in ch 5 par 5.5, particularly amendments brought about by the National Credit Amendment Act 19 of 2014.

¹³⁷ Although the South African legal system is a hybrid one, it subscribes to the principle of sanctity of contracts that typically forms part of civilian laws. See Otto 'General introduction' 6 as well as *Barkhuizen v Napier* 2007 (5) SA 323 (CC) and Otto and Prozesky-Kuschke 'Introduction to the law of contract' 42. See Kilborn 'Inaugural lecture' 2010 12–13 <http://bit.ly/1BoDJAP> (accessed 28 February 2015) on the development in European jurisdictions, starting from the notion that a discharge would be 'a scandalous abdication of responsibility' to the concept being generally accepted and a more nuanced and balanced understanding thereof.

¹³⁸ Spooner 2013 *ERPL* 779.

influence has an impact on policy. In South Africa, no real organised natural person debtor pressure/interest group exists. This is probably so since the 'richer' and therefore more publicly active insolvents already have a remedy in the form of the sequestration procedure at their disposal. Furthermore, the 'poor' do not interest lawyers and intermediaries (who will not benefit from reform and have an interest in protecting the current state of affairs) and therefore no organised pro-debtor interest groups are likely to arise from these corners.

When considering the need to reappraise the system from a debt relief perspective, it should be kept in mind that the assistance of individuals through, amongst others, the discharge of debt or the diversion of risk is not a foreign idea in South Africa. Furthermore, certain accounting practices recognise that some forms of debt are uncollectable and should be dealt with in a manner that reflects the true nature thereof.¹³⁹ In some instances, legislation directly makes provision for write-offs and deductions and in others, opportunities are created for people (with the means to do so) to safeguard themselves against situations that may result in their insolvency. In the first instance, write-offs – the most obvious example in the context of natural person insolvency law – are available to natural persons who form part of the higher tiers of the economy by means of the sequestration procedure. Another example from insolvency law is that in company law, when a company becomes insolvent, it is liquidated and creditors do not have a choice but to write off uncollectable debt. In such instance, creditors are usually not allowed to pursue the individuals that managed or owned the company and risk aversion is in fact one of the very reasons why companies and trusts are formed.¹⁴⁰ Other legislative measures used to protect individuals from undue financial risk are long- and short-term insurance.¹⁴¹ By taking out insurance, individuals are able to protect themselves from all types of risks such as sickness, theft, loss of income or natural disaster. Indeed, the very notion of insurance law is based on the realisation that there are inherent risks in life which fall

¹³⁹ South Africa prescribes to IAS (International Accounting Standards) as an auditing standard where unrecoverable assets, i.e. long outstanding debts, are impaired and then written off in accordance with IFRIS (International Financial Reporting Standards) to represent a fair value presentation – thereby acknowledging that some debts are truly unrecoverable.

¹⁴⁰ See Delpont *New entrepreneurial law* pts A and B.

¹⁴¹ See Long-term Insurance Act 52 of 1998 and Short-term Insurance Act 53 of 1998.

beyond an individual's control.¹⁴² From the above it is apparent that write-offs and risk diversion are not foreign to the South African financial sector. In contrast, existing legal instruments and constructions meant as safety features have an important role to play and are generally accepted. The possibility of furthering the development of these features also in natural person insolvency law therefore seems natural.

In linking the above practices to the call for a reappraisal of the insolvency system, it has to be noted that all the features discussed above are theoretically available to every natural person in South Africa. However, those forming part of the lower tiers of society cannot readily make use thereof due to a lack of education, skills and resources which at least renders a further consideration of safety nets within the auspices of insolvency law appropriate.

As the broader South African system seems to be out-dated and out of touch with modern trends it would be meaningful to investigate universal attributes of modern functioning systems that are responsive to modern day socio-economic needs.¹⁴³ As Spooner explains, policymakers should be more open to depart from legal traditions by embracing the reality that modern circumstances (of the consumer credit society) necessitate a radical reconsideration of legal convention.¹⁴⁴ Universal solutions should thus be considered for universal problems.¹⁴⁵

1.2 Research objectives

The research problem identified in the above discussion deals with the adequacy of natural person debt relief in South Africa and the way forward. The problem does not only relate to access to the system but also to the efficiency of existing debt relief

¹⁴² See Prozesky-Kuschke 'Insurance and carriage'.

¹⁴³ The American system was the first one to be based on economic principles. This approach has spilled over to and influenced reform in Europe: Huls 2012 *J Consum Policy* 498. See the discussion of the American system in ch 2 par 2.2.

¹⁴⁴ Spooner 2013 *ERPL* 787–789.

¹⁴⁵ See Ramsay 2012 *J Consum Policy* 427 who refers to developments in European systems as responses to changes in the economic and social environment. He mentions that these developments 'are functional responses to increased problems of over-indebtedness providing a safety net'. See further Boraine and Roestoff 2014 *THRHR* 546 as regards the South African system.

procedures, viewed both individually and holistically, in providing the diverse scope of overcommitted South African debtors with a viable prospect of a new start.¹⁴⁶ As stated by Van Heerden and Boraine,¹⁴⁷

the full spectrum of debt relief measures still needs further research with the view of establishing proper mechanisms with a clear application in order to deal with the variety of debt situations that may arise.

In summary the objectives of the study are therefore:

- a. to determine the current state of affairs with regard to debt relief for insolvent natural person debtors in South Africa;
- b. to address the question as to whether existing debt relief procedures provide adequate access to the natural person insolvency system;
- c. to address the question as to whether existing procedures provide efficient debt relief;
- d. to compare the South African natural person debt relief system with and to evaluate it against current international developments, principles and guidelines;
- e. to do a comparative study of other jurisdictions' natural person insolvency laws; and
- f. to make suggestions for law reform.

1.3 Delineation and limitations

The reasons for natural person insolvency and over-indebtedness and the prevention thereof are closely related and important to the research problem and objectives. However, in order to maintain focus and avoid a secondary chain of arguments, this study focuses on the treatment of insolvency and over-indebtedness of natural person debtors and does not in detail consider the reasons for its manifestation or the prevention of such occurrences.¹⁴⁸

¹⁴⁶ See ch 2 par 2.2 regarding the fresh start principle.

¹⁴⁷ Van Heerden and Boraine 2009 *PELJ* 58.

¹⁴⁸ See also *WB Report* 10. In the report, the treatment of insolvency and not the prevention thereof is addressed as it is noted that such related topics are complex and subject to substantial debate and disagreement which can form the subject of an entire separate study. Furthermore, Renke *An evaluation of debt prevention measures in term of the National Credit Act 34 of 2005* (LLD thesis University of Pretoria 2012) thoroughly addresses some of these matters.

Furthermore, although this thesis focuses on the very important plight of NINA debtors, its consideration forms part of the broader objective of this study, namely, the holistic reappraisal of the relief that the South African insolvency system offers to natural person debtors. The entire system needs to be reconsidered as one of the major points of criticism against it is its disorganised development which in itself brought about a myriad of difficulties within the debt relief sphere.¹⁴⁹ Also, although the trend to address the complications associated with NINA debtors by making use of specific procedures has in recent years led to reform in for instance Belgium,¹⁵⁰ Ireland¹⁵¹ and Scotland,¹⁵² a consideration of the latter two jurisdictions will not provide the same depth of analysis as the chosen comparative systems of New Zealand, England and Wales. The reason is that the chosen systems' NINA procedures have been available for a number of years during which their effectiveness could be evaluated more meticulously. As for Belgium, the contemplation of NINA procedures is but one of the focus areas of this thesis and the arguments as regards the reasons why New Zealand, and England and Wales were chosen for comparative purposes, as is set out more fully in paragraph 1.4, as well as language considerations,¹⁵³ have influenced my choice not to examine Belgian law in depth. In addition, the Belgian no-asset procedure will not further the discussions surrounding NINA debtors as it does not add to what the other, chosen systems offer.

Unfortunately, no empirical studies as regards the size of the South African NINA group of debtors are available. Inferences on the scope of the excluded group are therefore based on estimates.

¹⁴⁹ See chs 3 and 4 in general.

¹⁵⁰ As referred to above in par 1.1.

¹⁵¹ See the debt relief notice procedure in the Personal Insolvency Act No 44 of 2012. See further Spooner *Personal insolvency law* 95.

¹⁵² See the minimal asset process introduced by the Bankruptcy and Debt Advice Act 2014 which replaced the debt relief notice procedure.

¹⁵³ Some primary Belgian sources are only available in French with which I am not conversant.

1.4 Methodology

This research encompasses a literature study of legislation, case law, books, journal articles, theses and reports. As was indicated above,¹⁵⁴ the study is primarily a critical analysis of the South African state of affairs as regards natural person debt relief as measured against international trends, principles and guidelines.¹⁵⁵ A comparative study of pertinent aspects is undertaken by investigating the insolvency systems of New Zealand,¹⁵⁶ England and Wales.¹⁵⁷ The insolvency system of the United States of America is referred to as far as its philosophical undertone is concerned as it is regarded as the frontrunner in relation to debt relief in the form of a discharge.¹⁵⁸ Interesting French developments relating to an administrative approach are briefly explained.¹⁵⁹

New Zealand has recently reformed its insolvency law by amongst others introducing a new Insolvency Act.¹⁶⁰ Multiple procedures, namely, bankruptcy¹⁶¹ and alternative measures,¹⁶² in the form of proposals,¹⁶³ summary instalment orders,¹⁶⁴ and the no asset procedure¹⁶⁵ are provided for in this single Act. These procedures are devised in such a manner that no honest debtor is excluded from the system and all procedures lead to a discharge of debts. The New Zealand system is mostly administrative in nature and offers an uncomplicated structure. The system's simplicity and the fact that, in contrast with the South African position, it does not discriminate on financial grounds are attributes which render a comparative study especially attractive from a developing country's perspective. More specifically, and in line with the overall policy objectives of the system, the fairly recent development of introducing a specific debt relief measure for NINA debtors constitutes a major

¹⁵⁴ Para 1.1; 1.2 and 1.3.

¹⁵⁵ See ch 2 as regards international trends, principles and guidelines and chs 3, 4 and 5 regarding South African debt relief measures.

¹⁵⁶ See ch 6.

¹⁵⁷ See ch 7.

¹⁵⁸ In this regard it is interesting to note that comparative consumer insolvency law is at most only thirty-five years old as it was not regarded as a pressing social, legal and economic problem prior to the 1980s: Ziegel 2004–2005 *Penn St Int'l Rev* 639. See ch 2 par 2.2 as regards the American system.

¹⁵⁹ See ch 2 par 2.4.

¹⁶⁰ 2006.

¹⁶¹ See pt 2 in general.

¹⁶² S 8.

¹⁶³ Pt 5 sub-pt 2.

¹⁶⁴ Pt 5 sub-pt 3.

¹⁶⁵ Pt 5 sub-pt 4.

motivation for its consideration.¹⁶⁶ This is so as the majority of presently excluded debtors in South Africa form part of the NINA group.¹⁶⁷ Another reason for its choice is its commendable, all-encompassing approach in reconsidering its entire system at once and in line with clear principles.

The insolvency system in England and Wales is pro-debtor with some of its philosophical foundations being a discharge and the accompanying fresh start,¹⁶⁸ which its South African counterpart is sorely lacking. Although the system offers multiple procedures, all are not contained in a single statute. These procedures are bankruptcy¹⁶⁹ and alternative measures in the form of the individual voluntary arrangement procedure,¹⁷⁰ the county court administration order procedure¹⁷¹ and the so-called debt relief order procedure.¹⁷² As was mentioned above,¹⁷³ the latter procedure is of special interest as regards the present South African position as it specifically provides for the NINA category of debtors. The DRO became effective on 6 April 2009 and was inserted into the Insolvency Act through the Tribunals, Courts and Enforcement Act.¹⁷⁴ The system's pro-debtor approach and the multiple remedies that it offers, with emphasis on the recently developed DRO, coupled with the fact that English law greatly influenced South African insolvency law,¹⁷⁵ which has to some extent developed in a similar manner, justify its consideration. Evans correctly notes that the English policy driven reform 'can be of considerable value in an attempt to reform South African law'.¹⁷⁶ Lastly, although one of England's and Wales' debt relief procedures¹⁷⁷ is no longer suited to modern day needs and has consequently fallen into disuse, it has not led to a crisis as sufficient alternative

¹⁶⁶ See in general Coetzee and Roestoff 2013 *Int Insolv Rev* 209.

¹⁶⁷ *Idem* 189.

¹⁶⁸ Roestoff 'n *Kritiese evaluasie* 5.

¹⁶⁹ Pt 9 of the second group of parts of the Insolvency Act 1986.

¹⁷⁰ *Idem* pt 8.

¹⁷¹ This procedure is contained in pt 6 of the County Court Administration Act 1984, but has fallen in disuse: Spooner *Personal insolvency law* 90 n655.

¹⁷² Hereafter 'the DRO'. See pt 7A of the second group of parts of the Insolvency Act.

¹⁷³ Par 1.3.

¹⁷⁴ 2007.

¹⁷⁵ Roestoff 'n *Kritiese evaluasie* 8; Evans *A critical analysis* 13; and Maghembe *A proposed discharge* 114–115.

¹⁷⁶ Evans *A critical analysis* 13.

¹⁷⁷ The county court administration order procedure.

procedures exist – ensuring that all honest but unfortunate debtors have access to real debt relief.

1.5 Chapter overviews

- a. Chapter one provides background information and illustrates the need for further research in this field. The research objectives, delineations and limitations of the study as well as the method in which the research is conducted are also included in this chapter. The chapter also sets out the reference methods and important terms and definitions used throughout the thesis.
- b. Chapter two outlines the most important international trends, policy considerations, principles and guidelines relevant to this thesis. This framework is intended as a benchmark against which the South African system and those of New Zealand, England and Wales are measured in subsequent chapters.
- c. Chapter three considers the South African natural person debt relief measures contained in the Insolvency Act. Here, after a brief historical overview, the sequestration and statutory composition procedures are discussed and evaluated from a debt relief perspective. In this regard, the principles set out in chapter two as well as an evaluation of the advantage for creditors requirement in terms of the right to equality are important considerations. The discussions include considerations of the systemic consequences of the sequestration procedure's access requirements as well as the impact of secondary debt relief measures on applications for voluntary surrender.
- d. Chapter four is a discussion of the secondary statutory debt relief procedures in South Africa, namely, the administration order and debt review procedures stemming from the Magistrates Courts' Act and the NCA respectively. The same methodology followed in chapter three is employed as the measures are evaluated against the framework set out in chapter two and the right to equality. In this chapter, comments as regards the broader insolvency system's adequacy are made as, at that stage, all formal statutory procedures have been considered. Also, the discussion of equality is finalised as a conclusion is reached as to whether the broader South African natural person insolvency system unfairly and unjustifiably discriminates against certain categories of insolvent debtors.

- e. Chapter five offers a discussion of the proposed South African pre-liquidation composition procedure which was drafted with the intention of providing relief to those who are currently excluded from any and all statutory debt relief measures due to (direct and indirect) access requirements. The proposed procedure is measured against international guidelines, as set out in chapter two, and an investigation as to whether it would reach its goal is an important consideration. The chapter is further concerned with some ancillary debt relief measures. These are considered as their employment could possibly result in relief in one form or the other, although they cannot be categorised as and do not contain elements of conventional debt relief procedures. Furthermore, the primary and secondary debt relief procedures do not exist in a vacuum and therefore the study considers the extent to which this separate ancillary instruments impact on and possibly enhance the effectiveness of the primary and secondary procedures.
- f. Chapter six investigates the natural person debt relief landscape in New Zealand. Here, the jurisdiction's statutory measures are evaluated against international guidelines extracted in chapter two and compared to their South African counterparts where comparable procedures exist.
- g. Chapter seven deals with debt relief procedures for natural person debtors in England and Wales. As was done in chapter six, the different procedures are assessed in light of the international principles provided in chapter two and compared to their South African counterparts where it is competent to do so.
- g. Chapter eight provides conclusions as regards the adequacy and efficiency of the broader South African insolvency system from a debt relief perspective. In this chapter, relevant lessons from earlier discussions are extracted for South Africa and, most importantly, concrete recommendations for the way forward are made.

1.6 Reference methods, key references, terms and definitions

- a. The full titles of sources referred to in this thesis are provided in the bibliography, together with abbreviated 'modes of citation' which are used to refer to sources in footnotes. However, legislation is referred to in full.
- b. For the sake of convenience the masculine form is used throughout, unless specifically indicated otherwise.

- c. The South African Law Reform Commission was formerly known as the South African Law Commission. The new title will be referred to throughout this thesis.
- d. The law as stated in this thesis reflects the position as 30 April 2015.
- e. On 28 September 2015, the date on which this thesis was submitted for examination, the following applicable exchange rates applied:
 - 1 New Zealand dollar (NZD/\$) = 8.91 South African rand (ZAR/R)
 - 1 Great British pound (GBP/£) = 21.35 South African rand (ZAR/R)

f. Terms and definitions:

The INSOL *Consumer debt reports* note in their introduction to consumer debt problems that the term ‘consumer debtor’ is a misnomer as it makes no difference from the consumer debtor’s perspective whether debts are private or commercial in nature. It provides that¹⁷⁸

it is about individuals, natural persons, men and women, whose debts for which they are personally liable, however caused, (private or commercial) exceed their capacity to repay within a reasonable period.

Therefore, the terms ‘natural person debtor’ or ‘natural person insolvent’ are preferred. Reference to the term ‘consumer debtor’ will only be made where a particular publication under consideration makes use of the term.

‘Insolvency’ refers to a debtor’s financially troubled condition.¹⁷⁹ Insolvency and ‘over-indebtedness’ are used as synonyms in this study.

In South Africa and in the context of natural person debtors the term ‘insolvency law’ has a narrow meaning and generally refers to remedial measures contained in the Insolvency Act.¹⁸⁰ Internationally, the term ‘bankruptcy law’ is more commonly used and usually refers to laws relating to both individuals and companies or corporations. However, this is not a technical distinction.¹⁸¹ The term will, where applicable, be used as a synonym for ‘insolvency law’ although it will be restricted and used in the context of natural person debtors. Further as regards the use of the term ‘insolvency law’ in this study specifically, it is attributed a broader meaning and includes all

¹⁷⁸ INSOL *Consumer debt report* I 3 and INSOL *Consumer debt report* II 3.

¹⁷⁹ WB *Report* 5.

¹⁸⁰ See Bertelsmann *et al Mars* 16.

¹⁸¹ Rajak ‘The culture of bankruptcy’ 3.

natural person debt relief measures. In some instances, the culmination of procedures is also referred to as 'broader insolvency law'. Similarly 'insolvency procedures' refer to the collective procedures available to natural person insolvents which may contain a liquidation and repayment plan as well as no asset procedures.¹⁸² 'Bankruptcy procedures', 'insolvency procedures' and 'debt relief procedures' are considered to be synonyms for purposes of this thesis and are used interchangeably.

'Asset liquidation procedure' refers to a procedure where a debtor's non-excluded assets and everything in excess of his redemption capacity are sold and distributed amongst creditors, whereupon a discharge is provided for unpaid balances.¹⁸³

'Rehabilitation procedure' refers to a procedure which provides a debtor with some time to recover from permanent or temporary liquidity problems. It provides a measure through which a debtor can reorganise his financial affairs.¹⁸⁴ In this respect the terms 'rehabilitation procedure' and 'repayment plan procedure' are used interchangeably and as synonyms in this study.

'Debt counselling' is generally used to refer to some method of mediation prior to the invocation of formal procedures. It is aimed at solving debt problems.¹⁸⁵ In South Africa, the term is also in practice used as a synonym for the 'debt review' procedure.¹⁸⁶

'Discharge' is the resultant release from obligations to service debt which stems from the invocation of insolvency procedures.¹⁸⁷

'Open access' refers to systems where individuals who meet an insolvency test, such as the inability to pay debts as they fall due, may without more gain access to

¹⁸² INSOL *Consumer debt report* I 3.

¹⁸³ INSOL *Consumer debt report* I 9 and INSOL *Consumer debt report* II 12.

¹⁸⁴ INSOL *Consumer debt report* I 9 and INSOL *Consumer debt report* II 11.

¹⁸⁵ INSOL *Consumer debt report* I 8 and INSOL *Consumer debt report* II 11.

¹⁸⁶ See ch 4 par 4.3.

¹⁸⁷ INSOL *Consumer debt report* I 6 and INSOL *Consumer debt report* II 9.

an insolvency procedure that allows an ultimate discharge of debts.¹⁸⁸ It may in some contexts also refer to systems where the debtor has a choice as regards his preferred debt relief measure.¹⁸⁹

‘Trustee’ or ‘administrator’ refers to an individual or organisation selected to administer the assets and/or income of the debtor and to distribute proceeds to creditors.¹⁹⁰ The terms ‘insolvency (bankruptcy) representative’ and ‘insolvency practitioner’ are used as synonyms for ‘trustee’ or ‘administrator’.

The reference to ‘NINA’ includes ‘LILA’ as it does not only refer to literally no income and no assets, but also to insufficient attachable assets and income to contribute towards debt.¹⁹¹

¹⁸⁸ WB *Report* 134.

¹⁸⁹ See the American Pre-Bankruptcy Abuse Prevention and Consumer Protection Act of 2005; ch 2 par 2.2.

¹⁹⁰ INSOL *Consumer debt report* I 7.

¹⁹¹ See par 1.1.

CHAPTER 2: INTERNATIONAL TRENDS AND GUIDELINES

SUMMARY

- 2.1 Introduction
 - 2.2 The fresh-start policy, an American invention
 - 2.3 European recommendations
 - 2.4 An innovative administrative approach in France
 - 2.5 INSOL international consumer debt reports
 - 2.6 World Bank Report on treatment of the insolvency of natural persons
 - 2.7 Conclusion
-

2.1 Introduction

It was established in chapter 1¹ that national factors should not be over-emphasised when a jurisdiction's natural person insolvency system is reviewed and that policymakers should be more open to depart from legal traditions by embracing the reality that modern needs (of the consumer credit society) necessitate a radical reconsideration of legal convention.² Universal modern solutions should thus be considered for universal modern realities.³ In this regard, the remarks of Vijay Tata⁴ at the closing of the World Bank Insolvency and Creditor/Debtor Regimes Task Force meeting on 11 January 2011 are to the point:⁵

[O]ne of the lessons from the recent financial crisis was the recognition of the problem of consumer insolvency as a systemic risk and the consequent need for the modernization of domestic laws and institutions to enable jurisdictions to deal effectively and efficiently with the risks of individual over indebtedness. The importance of these issues to the international financial architecture that has been recognized in various ways by the G-20 and Financial Stability Board

¹ See par 1.1.

² Spooner 2013 *ERPL* 787–789.

³ See Ramsay 2012 *J Consum Policy* 427 who refers to developments in European systems in response to changes in the economic and social environment. He mentions that these developments 'are functional responses to increased problems of over-indebtedness providing a safety net'.

⁴ Chief counsel at the World Bank.

⁵ See <http://bit.ly/1D1cMoc> (accessed 29 March 2015).

has today been reconfirmed and emphasized by this Task Force. It is important to recognize the diversity of policy perspectives, values, cultural preferences and legal traditions that shape the way jurisdictions may choose to deal with the problems of individual over indebtedness. Yet recent events suggest that the expansion of access to finance, the extension of modern modes of financial intermediation, and the mobility and globalization of financial flows may have changed the character and scale of the risk of consumer insolvency in *similar ways* in many different economies.⁶

As natural person insolvency is a universal problem, various international best practices, principles and guidelines have been established in this regard. It is paramount to investigate international recommendations in order to depict the context in which modern natural person insolvency finds itself, but more importantly to establish what are presently regarded as good and solid foundations of an insolvency system as a response to contemporary needs. The main aim of this chapter is therefore to consider some of the more pertinent and recent international principles and guidelines relating to natural person insolvency, which can be regarded as being equally relevant in all jurisdictions, in order to establish the most commonly shared recommendations made by the international community. Principles and guidelines that focus specifically on natural person insolvency are considered in detail, whilst those focused on business insolvency are limited to subtexts. The most prominent international reports relating to natural person insolvency at present are the INSOL International⁷ *Consumer debt reports*⁸ and the World Bank *Report on the treatment of the insolvency of natural persons*.⁹ Where necessary, reference is made to the unified standard developed by the World Bank for the comparative examination of business insolvency and creditor/debtor regimes.¹⁰ However, before considering specific international recommendations, some of the developments in the United States of America,¹¹ the broader European context and France are briefly considered. A brief consideration of developments in the USA and the broader European environment provides a background to some of

⁶ My emphasis.

⁷ International Federation of Insolvency Professionals (hereafter 'INSOL').

⁸ INSOL *Consumer debt report I* and INSOL *Consumer debt report II*.

⁹ *WB Report*.

¹⁰ Hereafter 'The ICR standard'. This standard comprises of the WB *Principles* and the UNCITRAL *Guide*.

¹¹ Hereafter the 'USA' or 'American'. See Roestoff *in Kritiese evaluasie* ch 5; Evans *A critical analysis* ch 6; Steyn *Statutory regulation 422 et seq*; and Maghembe *A proposed discharge* 175 *et seq* for a more detailed analysis of the American system.

the most important international guidelines discussed later. The progress made in France as regards the administration of an insolvency system is briefly discussed. The French system's introduction of innovative measures to reduce its administrative burden without compromising debt relief cannot be ignored from a developing country's perspective and therefore brief reference is made to some of the latest reforms in this regard.

As regards the structure of this chapter, paragraph two considers the fresh start principle which had its origin in the USA in the 1980s and is widely regarded as having liberalised the field of natural person insolvency law. Some of the most prominent European reports on the subject are referred to in paragraph three. Paragraph four reflects on administrative developments in France. However, the discussions in paragraphs two to four are not meant to be detailed analyses. Paragraphs five and six deal with the heart of this chapter, namely, a discussion of the most eminent international principles and guidelines. In this regard, paragraph five deals with the INSOL reports and paragraph six considers the World Bank *Report*. Paragraph seven extracts the basic elements or conceptual parts of an efficient and effective natural person insolvency regime, which is intended as a framework against which systems are measured later in this thesis. The paragraph also concludes this chapter.

2.2 The fresh-start policy, an American invention

The fresh-start policy has its origins in the USA where natural person insolvents can apply it to their advantage by making use of the provisions of the Bankruptcy Reform Act of 1978.¹² The policy is central to the modern USA bankruptcy system of which

¹² Hereafter the 'Bankruptcy Code'. See Kilborn 2009 'Bankruptcy law' <http://bit.ly/1EfD9rz> (accessed 28 February 2015) regarding the earlier history of bankruptcy in the USA. See Roestoff *in Kritiese evaluasie 172 et seq* and Maghembe *A proposed discharge 37 et seq* for detailed discussions of the USA fresh-start policy.

the primary goal (still)¹³ is to provide debt relief¹⁴ to all honest but unfortunate debtors.¹⁵ Van Apeldoorn describes the system as one where it¹⁶

is not a favour, but an (almost) automatic right to be discharged from pre-bankruptcy debts in a fairly quick and formal bankruptcy proceeding.

The theoretical basis of the American fresh-start policy is examined first whereafter the actual procedures are briefly set out. Gross describes the fresh start as the manner in which¹⁷

society (through the bankruptcy system) mandates that creditors and other members of society forgive nonpaying debtors.

She continues to explain that forgiveness, amongst others,¹⁸

gives the wrongdoer (the debtor) the opportunity to regain self-esteem and become once again a productive member of society. In a capitalistic economy, we want debtors to reintegrate into the system for their sake and our own. For debtors, reintegration allows the taking of new risks. For society, taking risks is exactly what we want individuals and businesses to do. This enables the wheel of commerce to turn; individuals fend for themselves and do not become a drain on scarce societal resources.

In the USA, a fresh start is accomplished by means of two main mechanisms. The first is a discharge from debts which is the single most important aspect for debtors. The second is the debtor's ability to retain 'exempt' property which improves the outcome of the discharge in that debtors are provided with the necessities to carry on with their lives.¹⁹ In this respect Ferriell and Janger's explanation of the philosophy behind the discharge links with Gross' description of what forgiveness entails as they explain that²⁰

¹³ In light of the reforms discussed below.

¹⁴ Huls 2012 *J Consum Policy* 499. See also Epstein and Nickles *Bankruptcy law* 7 and Evans *A critical analysis* 151 and 154.

¹⁵ *Local Loan Co v Hunt* 1934 292 US 244. Prior to the 2005 amendments to the bankruptcy system noted below, the American system was described as ultra-liberal; Ziegel 2004–2005 *Penn St Int'L Rev* 645. The ultra-liberal approach stands in stark contrast to the present South African system that can be categorised as very conservative in its response to natural person insolvencies; see ch 1 par 1.1.

¹⁶ Van Apeldoorn 2008 *Int Insolv Rev* 66.

¹⁷ Gross *Failure and forgiveness* 93.

¹⁸ *Idem* 94.

¹⁹ Ferriell and Janger *Understanding bankruptcy* 4.

²⁰ *Ibid.*

[f]reed from their past obligations debtors have a renewed incentive to engage in economically productive efforts knowing that they will be able to retain the fruits of their revived efforts.

The above citations tie in with the ‘rehabilitation’ theme, one of three traditional justifications for the fresh-start policy and by far the most common, as noted by Kilborn.²¹ He argues that three theoretical justifications have developed as the notion of allowing people to escape their obligations seems to be contradictory. This is so as it infringes the most basic principle underlying the law of contract, namely, *pacta sunt servanda*.²² The other two themes are the ‘mercy’ theme,²³ which is entrenched in morality and basic humanity and calls on the law to show compassion and mercy to honest but unfortunate debtors who suffer without reason, and the ‘collection’ or ‘creditor protection’²⁴ theme which is the oldest and which can be described in the following terms:²⁵

[T]he prospect of a discharge is supposed to encourage the debtor to cooperate with her creditors to reveal property available to pay debts, avoid a wasteful multiplicity of collection actions by various creditors, and provide for generally equal distribution of the debtor’s property among all creditors.

In the context of the USA, Kilborn disapproves of the ‘collection’ theme as natural person debtors have little to offer for collection and distribution.²⁶ Although the ‘mercy’ theme made sense in times of debt slavery and imprisonment, it should also be discarded as it has lost its substance in recent times as a result of contemporary debt collection restrictions and the protection of debtors’ personal liberty.²⁷ Kilborn concludes that the ‘rehabilitation’ theme is also generally overstated due to modern laws of debtor protection which, amongst others, provide for the organisation of business to shield individuals from financial risk and to encourage entrepreneurship.

²¹ See Kilborn 2003 *Ohio St LJ* 862–864 and 877. See also his examination of the themes 864–883.

²² *Idem* 861. See Christie and Bradfield *Christie’s* 12 in relation to the principle which means that agreements must be honoured (and that courts will enforce contracts).

²³ Kilborn 2003 *Ohio St LJ* 863.

²⁴ For similarities in the South African system see ch 1 par 1.1.

²⁵ Kilborn 2003 *Ohio St LJ* 862.

²⁶ *Idem* 865–866.

²⁷ *Idem* 866–876. Slavery was abolished throughout the British colonies, including South Africa, in 1834 by means of the Slavery Abolition Act of 1833. The imprisonment for debt was set aside in South Africa in 1995 following the decision of the Constitutional Court in *Coetzee v Government of RSA; Matiso v Commanding Officer, Port Elizabeth Prison* 1995 (4) SA 631 (CC). See further Roestoff and Renke 2003 *Obiter* 10–11.

In this regard an individual can form a company or a close corporation²⁸ to transfer such risks and he is further protected by laws providing for the exemption of property, including wages, from the insolvent estate.²⁹ Although Kilborn acknowledges that these laws do not provide total protection, he argues that the remaining needs are disproportionate to the level of relief offered by the individual bankruptcy law (as it stood at the time).³⁰ In line with the sentiments expressed by Kilborn, many non-American observers are uncomfortable with the ultra-liberal fresh-start policy and regard it as excessively generous and naïve.³¹

As far as the actual debt relief procedures leading to a discharge are concerned, the Bankruptcy Code offers access to the fresh start by means of two procedures. These are liquidation under chapter 7³² and rehabilitation under chapters 11³³ and 13.³⁴ The filing of a petition by the debtor commences proceedings and he does not have to be insolvent to access the system.³⁵ Chapter 7 contains the most common form of bankruptcy, previously referred to as ‘straight bankruptcy’,³⁶ and petitions may be filed both involuntarily³⁷ and voluntarily³⁸ although voluntary filings are the most common.³⁹ The debtor who files for bankruptcy must surrender all non-exempt property to the trustee and he receives an immediate and unconditional discharge in exchange.⁴⁰ The trustee sells the property and distributes the proceeds to

²⁸ Due to levels of education and resources, this option is not available to the so-called No Income No Asset (NINA) debtors in South Africa; see ch 1 par 1.1. Furthermore, in South Africa, credit providers generally require directors of companies to personally guarantee the debt of juristic persons by signing surety agreements.

²⁹ Kilborn 2003 *Ohio St LJ* 876–883. Kilborn argues that, in contemporary individual bankruptcy, the protection of future wages seems to be the only remaining compelling argument for the rehabilitation theme. In South Africa no maximum percentage of an individual’s salary/wage that may be attached by means of an emoluments attachment order is set; ch 1 par 1.1. See also in general Evans *A critical analysis* as regards South African exemption laws.

³⁰ Kilborn 2003 *Ohio St LJ* 876.

³¹ See Ziegel 2004–2005 *Penn St Int’L Rev* 646 and authorities cited there. See also the pro-liberal arguments noted by Ziegel 647–648.

³² See ss 701–784.

³³ See ss 1101–1174. Ch 11 provides for a reorganisation process similar to that of ch 13. However, the ch 11 process is more expensive and complicated than ch 13 and therefore generally only used by businesses; Ferriell and Janger *Understanding bankruptcy* 191.

³⁴ See ss 1301–1330.

³⁵ Huls 2012 *J Consum Policy* 498–499.

³⁶ See Evans *A critical analysis* 153. See also Kilborn 2003 *Ohio St LJ* 856–857 and Ferriell and Janger *Understanding bankruptcy* 603.

³⁷ S 303(a).

³⁸ S 301.

³⁹ Evans *A critical analysis* 157.

⁴⁰ S 727. See Kilborn 2003 *Ohio St LJ* 857.

creditors.⁴¹ Chapter 7 has two goals, namely, liquidation of the debtor's assets and the granting of a discharge. There is no link between eligibility for a discharge and the amount which creditors receive, but the discharge relates only to unsecured debts. In the latter regard, the debtor has a choice to pay secured debts, sign reaffirmation agreements⁴² or surrender the property that serves as security.⁴³

Chapter 13 provides for the rescheduling of debts of an individual with a steady and regular source of income.⁴⁴ This procedure may only be initiated voluntarily. It entails a payment plan in terms of which future income is utilised for the total or partial satisfaction of claims. However, maximum thresholds of debt liability in respect of both secured and unsecured claims are provided for.⁴⁵ The maximum duration of a repayment plan is usually not more than three years although a court may approve a plan for a longer period, but never for longer than five years.⁴⁶ The debtor need not surrender his assets as is the case in terms of chapter 7 bankruptcy. A chapter 13 discharge is only granted when the debtor has made full payment in terms of the payment plan.⁴⁷ Nevertheless, a debtor may request a chapter 13 'hardship discharge'. In such a case the court may only grant a discharge if⁴⁸

- a. the debtor's failure to complete the plan is due to circumstances for which the debtor should not be held accountable;
- b. the creditors have received at least the liquidation value of their unsecured claims; and
- c. modification of the plan is not practicable.

⁴¹ S 726.

⁴² Reaffirmation, in essence, entails a promise by the debtor to pay a debt despite its discharge. Reaffirmations are apparently only appropriate when a debtor is in arrears with payments of secured debts and does not wish to pursue ch 13 to deal with the problem. Acceptance of the offer of reaffirmation enables the debtor to keep the encumbered property and pay the debt over time. Reaffirmations of unsecured debts would seldom (if ever) benefit debtors; see Boraine and Roestoff 2000 *Obiter* 49 and authority cited there.

⁴³ See in general Ferriell and Janger *Understanding bankruptcy* 603.

⁴⁴ See s 101(30) and the title of ch 13: 'Adjustment of debts of an individual with regular income.'

⁴⁵ S 109(e).

⁴⁶ S 1322(d).

⁴⁷ S 1328.

⁴⁸ S 1328(b). The American hardship procedure could be considered in an investigation of how to deal with South African consumers who have accessed a repayment plan, but who have subsequently become NINA debtors. See ch 4 par 4.2 and 4.3 as regards the South African statutory repayment plan procedures.

A discharge (in terms of chapters 7 and 13) serves as a prohibition against any attempt to collect, recover or offset any discharged debt as a personal liability of the debtor.⁴⁹

The Bankruptcy Code does not base the right to a discharge on a certain level of payment to creditors and was, until 17 October 2005,⁵⁰ completely open to access. However, the BAPCPA has revised the very liberal ‘fresh-start’ philosophy of the American system by denying the debtor immediate (or straight) relief under chapter 7 in instances where it appears that he will be able to pay a portion of his debt from future income. BAPCPA, amongst others, introduced compulsory counselling⁵¹ and a means test⁵² to determine whether a debtor qualifies for chapter 7 bankruptcy or whether he should rather follow the chapter 13 route. Nevertheless, the means test should only be applied when the consumer’s gross income exceeds the median income in his state of residence.⁵³

BAPCPA obviously had a drastic impact on the extremely liberal open-access USA bankruptcy system in that it curtailed the fresh-start principle in certain respects.⁵⁴ This development was met with criticism as, amongst others, many believe that BAPCPA’s ‘crusade’ to prevent abuse and fraud penalises many honest but unfortunate debtors.⁵⁵ In this regard Kilborn describes the reform as a ‘spectacular failure’ and refers to commentators who cogently argue that BAPCPA has contributed to the subprime foreclosure crisis and the meltdown of the housing market which spread globally. He also provides statistics which clearly show that the reform did not solve the supposed problem of excessive consumer filings, which could possibly disprove the hypothesis that significant numbers of potential abusers are now opting for chapter 13 repayment plans or do not access the system at all.⁵⁶ He further argues that the compulsory introduction of the means test has led to

⁴⁹ S 524.

⁵⁰ This was the date on which the majority of the provisions of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (hereafter ‘BAPCPA’) came into effect.

⁵¹ S 109(h).

⁵² S 707(b)(2).

⁵³ See Calitz 2007 *Obiter* 399 and 405 *et seq.*

⁵⁴ See Van Apeldoorn 2008 *Int Insolv Rev* 72.

⁵⁵ Calitz 2007 *Obiter* 407–408.

⁵⁶ See Kilborn 2012 *Loy Consumer L Rev* 4–5.

excessive paperwork and a heavy burden of monitoring compliance which were all for naught. Kilborn goes so far as labelling the entire means test enterprise as a 'fool's errand'. This is because only 1% of chapter 7 filings have been found to be 'abusive'.⁵⁷ However, despite the more conservative application of the fresh-start principle in the USA as of late, Roestoff correctly remarks that the system can still be regarded as pro debtor as it continues to provide alternative relief, in the form of chapter 13, to those who do not qualify for a discharge in terms of chapter 7.⁵⁸

2.3 European recommendations

A wealth of studies and recommendations have originated in the field of natural person debt relief in Europe over the past 25 years. The aim of this discussion is not to analyse these voluminous studies and reports in detail, but to describe the broader policy developments in the European context by briefly referring to the most authoritative works. This will show that all of these commentaries are proponents of similar core principles.⁵⁹

As no study of European natural person insolvency law would be complete without a reference to the still influential 'Cork Report', the European journey starts on 27 January 1977. On this date, the first comprehensive and official review of the law of insolvency in more than a century was initiated in England and Wales through the establishment of the Cork committee.⁶⁰ The terms of reference were unparalleled at

⁵⁷ In concluding his evaluation of the USA reform Kilborn makes the following statement *idem* 12–13:

The losses from this ill-conceived and poorly implemented reform continue to mount with no end in sight. From a social policy perspective, BAPCPA represents an enormous step backwards, a regulatory response that has made treating the casualties of financial market risks all the more expensive and cumbersome. Indeed, as usual, the most financially distressed and socially excluded suffer the most, as one of the greatest tragedies of the U.S. reform was a market rise in the cost of retaining an attorney to guide debtors through this now even more complex thicket of rules and traps. Many debtors who need and deserve relief are now priced out of this 'market'. These problems will likely plague the U.S. system for years to come.

⁵⁸ See Roestoff *in Kritiese evaluasie* 240–241. Her observations were in light of the proposed amendments to the Bankruptcy Code which has since become law in the form of BAPCPA.

⁵⁹ Kilborn 'Inaugural lecture' 2010 2 <http://bit.ly/1BoDJAP> (accessed 28 February 2015; hereafter 'Inaugural lecture')

⁶⁰ Cork Report iii and 9.

the time and the committee's final report titled *Insolvency law and practice* was published in June 1982.⁶¹

Although the report is no longer contemporary, many of its outcomes are still relevant today. Some of the premises on which it was based are that insolvency law should be aligned with the realities of society and commercial life of the time;⁶² that it is important to discipline dishonest or reckless insolvents, but also to create a system that deals sympathetically with the 'honest though unfortunate' debtor;⁶³ and that a just balance must be maintained between creditors, the debtor and society.⁶⁴ The report contains many detailed recommendations. The principal ones as extracted by Fletcher⁶⁵ are that a unified insolvency code is preferred;⁶⁶ that an integrated system of insolvency courts should be established to administer the law;⁶⁷ that the role of the official receiver must be maintained and strengthened;⁶⁸ and that private insolvency practitioners should be regulated.⁶⁹ In addition, a number of novel procedures, which would serve as alternatives to bankruptcy, depending on differing circumstances and merits, were proposed.⁷⁰ One of the committee's observations clearly mirrors its stance as regards debtor applications. It provides as follows:⁷¹

We are firmly of the view that, where appropriate, debtors should be encouraged to file their own Applications, and that the process should be as simple, swift and cheap as can be devised.

Another prominent, early study was undertaken by Huls in 1991–1992 on behalf of the European Commission. In the report titled *Overindebtedness of consumers in the EC member states: Facts and search for solutions*⁷² Huls took cognisance of the principles of the *Cork Report*, with Kilborn noting that several consumer-specific

⁶¹ See *Cork Report* front page. See also in general Fletcher *The law of insolvency* 15–22.

⁶² *Cork Report* par 3, 8, 11 and 198.

⁶³ *Idem* par 23 and 198.

⁶⁴ *Idem* par 24 and 198.

⁶⁵ See Fletcher *The law of insolvency* 19.

⁶⁶ See *Cork Report* ch 10 par 538 *et seq.*

⁶⁷ See *idem* ch 20.

⁶⁸ See *idem* ch 14.

⁶⁹ See *idem* chs 15 and 16.

⁷⁰ See *idem* chs 6, 7, 11 and 13.

⁷¹ *Idem* par 539.

⁷² Hereafter '*Huls Report*'. For summaries of the report see Huls 1993 *J Consum Policy* and Kilborn 'Inaugural lecture' 2–4.

principles thereof had set the background for the Huls study.⁷³ In line with the *Cork Report*, the *Huls Report* recognises the importance of balancing the interests of creditors, debtors and society.⁷⁴ In order to maintain this balance, the *Huls Report's* recommendations centre on the principle that a debtor must do the best that he can towards servicing his debt for a restricted period.⁷⁵ In this regard, his non-exempt assets and net earnings, after essential expenses have been deducted, should be used and once the restricted period has run out, the consumer must be discharged from most of the remaining debt.⁷⁶ The report recommended that 'legislation must prescribe an orderly procedure of debt settlement and also provide for the basic elements of the substantive aspects'.⁷⁷ Six successive procedural steps were deemed important, namely:⁷⁸

- a. A stay of creditors' collection efforts;
- b. the preparation of a plan by the debtor and debt counsellor⁷⁹ for the payment of all creditors. Disposable income and non-exempt goods provide the basis for the redemption scheme. Proposals should be realistic and payment should be made from the moment the plan is formulated;
- c. the feasibility of the plan must be decided by a judge, although the plan must be discussed with creditors with the object of approval. A cram down of 75% is proposed. If no agreement can be reached, the matter should be referred to court for approval and the court should also appoint an administrator;⁸⁰
- d. the period should not exceed four years;
- e. the procedure should end as stipulated in the plan, when the judge declares a discharge;⁸¹ and

⁷³ See Kilborn 'Inaugural lecture' 2 and Huls 1993 *J Consum Policy* in general.

⁷⁴ See Huls 1993 *J Consum Policy* 220–224.

⁷⁵ *Idem* 221.

⁷⁶ *Idem* 225–226.

⁷⁷ *Idem* 225.

⁷⁸ *Idem* 225–227.

⁷⁹ The report emphasised that financial counselling needs to be specialised and that professional counsellors need, amongst others, to have knowledge of legal, financial and social aspects; *idem* 229–232.

⁸⁰ Debt counsellors could be appointed as such provided that their independence and professionalism are guaranteed; *idem* 232.

⁸¹ Alimony and liabilities as a result of criminal intent or gross negligence should not be discharged. Jurisdictions should also decide on an exemption scheme as regards income and assets; *idem* 229. Furthermore, credit agreements entered into during the plan without the plan administrator's consent cannot be discharged.

- f. the aftermath should be provided for in that creditors who attempt to have their discharged debt settled should be viewed with scepticism and the voluntary settlement of discharged debt should not be encouraged.

As regards the substantive law, the report suggested that the debt settlement process must meet certain legal requirements. These are the debtor's best efforts (however, 'best efforts' do not exclude those with zero redemption capacity); significant flexibility as regards the period of repayment – within a maximum period of four years; a classification of creditors by firstly providing for costs of proceedings, then secured debt, followed by preferential debts and finally unsecured debts; longer term commitments such as rent or electricity should be considered; and generally no interest should be charged from the moment the plan is filed.⁸²

Other important aspects covered by the report relate to the question of who should foot the bill and the need for professional and independent debt counsellors. In the former regard it is highlighted that costs should not constitute a barrier to accessing debt relief. As all parties benefit from the procedure, all should contribute, including creditors as their interests are protected by the procedure.⁸³ As far as the independence of debt counsellors is concerned, it is of the utmost importance that creditors should not dominate the supervising bodies of debt counselling agencies.⁸⁴

In 2003, a decade after the *Huls Report* was tabled, the European Union ordered a study on *Consumer overindebtedness and consumer law in the European Union*. Huls again formed part of the team, although the research was led by Reifner.⁸⁵ It drew extensively from the first *INSOL Consumer debt report* (discussed below)⁸⁶ and acknowledges that the report 'presents the international consensus about sound law and policy in insolvency matters'. Consequently, the *Reifner Report* regards the *INSOL Report's* principles as presenting a sound foundation on which European scholars and practitioners can build.⁸⁷ The report described the evolving European

⁸² *Idem* 227–229.

⁸³ *Idem* 232.

⁸⁴ *Idem* 233.

⁸⁵ See the summary of the *Reifner Report* by Kilborn 'Inaugural lecture' 6–8.

⁸⁶ Par 2.5.

⁸⁷ *Reifner Report* 45 and 249.

systems at the time, but was hesitant to choose one as representing best practice.⁸⁸ However, it identified nine principles of the European natural person insolvency approach (at the time). These are:

1. 'Consumer insolvency law' recognises the importance of preventative measures, but emphasises the importance of insolvency laws as a remedy where 'the debt burden has become unbearable'.⁸⁹
2. A '[d]ischarge' should be possible and as wide as possible, but may be partial so that the debtor is required to pay a part of the debt.⁹⁰ Payment should be adjusted to the debtor's means. However, a total discharge in hardship cases should be allowed. Although exceptions for taxes, fines and damages are not recommended, the priority of alimonies for children is recognised. Open access is preferred and should be denied only in cases of fraud or serious misconduct.
3. 'Preference for informal and out-of-court settlements' is expressed.⁹¹ In this regard access to adequate legal aid or counselling is important. Some form of court supervision and the possibility of approaching the court are mentioned as factors that would strengthen out-of-court settlements. Specific measures are proposed for situations where creditors resist settlements or remain passive.
4. A '[c]ourt procedure' should be possible where a voluntary settlement is not reached and should lead to a discharge.⁹² Simplified procedures are preferred.
5. 'Consideration for guarantors' who have provided personal guarantees for debtor's loans or provided assets as collateral is proposed. However, it is recognised that a satisfactory solution has not been developed.⁹³
6. 'Protection of assets and income' by respecting the right to a decent living standard for the debtor and his family.⁹⁴ The report is hesitant to recommend the protection of cars or homes.
7. A 'reasonable time frame' is important⁹⁵ and in this regard a period of three years is preferred.⁹⁶

⁸⁸ See Kilborn 'Inaugural lecture' 7.

⁸⁹ Reifner *Report* 250.

⁹⁰ *Ibid.*

⁹¹ *Idem* 250–251.

⁹² *Idem* 251.

⁹³ *Idem* 251–252.

⁹⁴ *Idem* 252–253.

⁹⁵ *Idem* 253–254.

8. 'Non-discrimination' in that the discharge should provide full access to financial activity.⁹⁷ A clear statement should be included in legislation to curb such practices in for instance the labour market and as far as access to housing is concerned. The need for special regulation of credit information registries is mentioned. It is recommended that completed payment plans should be expunged from the registries.
9. 'Availability of counselling and legal aid' in both out-of-court and court procedures is important.⁹⁸ The roles of a counsellor and the trustee should be kept separate and be performed by different individuals.⁹⁹

The report highlights the need for equipped, professional and independent debt counselling.¹⁰⁰ As regards funding, the sentiment is expressed that all parties benefit from the work of the debt counsellor and therefore all should contribute a reasonable share. The debtor should pay a limited amount and it is stated that there are strong arguments for financial support from governments as public interests are served by the counselling process. Creditors should also contribute as their interests are protected in that one creditor is prevented from enforcement at the expense of the others. Debt counsellors further play a monitoring role which is something that creditors would have had to do themselves.¹⁰¹

Also in 2003, the European Commission's enterprise directorate published the 'best project' report on restructuring, bankruptcy and a fresh start.¹⁰² Although its focus is on business insolvency and bankruptcy, it contains recommendations that are equally important to natural person insolvency law.¹⁰³ The significance that the report attaches to the fresh start of non-fraudulent debtors is important. In this regard it recommends, amongst others, an early discharge and that the stigmatising effects of bankruptcy be reduced by for instance removing obsolete and damaging restrictions,

⁹⁶ Kilborn 'Inaugural lecture' 8 notes that the proposed maximum time frame goes further than the first INSOL report and the Huls *Report*.

⁹⁷ Reifner *Report* 254.

⁹⁸ *Ibid*.

⁹⁹ Contra Huls *Report*. See Huls 1993 *J Consum Policy* 232.

¹⁰⁰ Reifner *Report* 256–258.

¹⁰¹ *Idem* 285.

¹⁰² EC *Best project report*.

¹⁰³ See Kilborn 'Inaugural lecture' 8.

disqualifications and prohibitions.¹⁰⁴ As far as the system itself is concerned, the report was in favour of simplified and less costly procedures and also proposed the development of specialised insolvency sections in courts.¹⁰⁵

In response to the growing problem of natural person over-indebtedness in member states of the Council of Europe,¹⁰⁶ Niemi-Kiesiläinen was commissioned by the European ministers of justice to prepare a report on *Legal solutions to debt problems in credit societies*.¹⁰⁷ The study recognised the Reifner *Report*, of which Niemi-Kiesiläinen was an author, as an important source.¹⁰⁸ It was published in October 2005 and made the following recommendations as regards 'judicial debt adjustment for consumers':¹⁰⁹

- (a) the debt adjustment should be accessible to debtors who have acted in good faith towards the creditors;
- (b) the debtor should have access to cost-free assistance in the procedure;
- (c) the debt adjustment procedure should be cost-free or low cost;
- (d) the payment plans in debt adjustment should be reasonable both in payment obligations and in length;
- (e) the debt adjustment should cover the debtor's all debts, excluding the maintenance payments to a debtor's child;
- (f) the debtor and creditors should be encouraged to make a voluntary agreement on the payment of the debts and passive creditors should not be allowed to hinder such an agreement;
- (g) the rights of the private guarantors of the debtor's debts should be recognised in the debt adjustment procedure.

In response to the Niemi-Kiesiläinen report, further reports were prepared¹¹⁰ which were followed by recommendations for adoption by the Council of Europe.¹¹¹ These recommendations were adopted on 20 June 2007 by the committee of ministers and the fourth recommendation, titled 'Introduce mechanisms necessary to facilitate rehabilitation of over-indebted individuals and families and their reintegration into society' largely follows the Niemi-Kiesiläinen *Report*. In a nutshell it is recommended

¹⁰⁴ EC *Best project report 28*.

¹⁰⁵ *Idem 27*.

¹⁰⁶ The CoE is not an organisation of the EU and should not be confused with the EC and the Council of the EU. The CoE promotes co-operation between European countries. It is mainly concerned with human rights issues and makes recommendations although such recommendations do not have any legal standing.

¹⁰⁷ Niemi-Kiesiläinen *Report*.

¹⁰⁸ *Idem 5*.

¹⁰⁹ *Idem 42*.

¹¹⁰ See Kilborn 'Inaugural lecture' 10.

¹¹¹ Recommendations CM/Rec (2007) 8.

that debtors should have effective access to impartial advice and debt adjustment; payment plans should be reasonable in both repayment obligations and duration; all debts should be covered (excluding special waivers under national laws); mechanisms for extra-judicial settlements should be established and encouraged; creditors' ability to unreasonably hinder settlements should be limited; effective financial and social inclusion of debtors (and their families) should also be encouraged – specifically their access to the labour market; active debtor participation in debt settlements and pursuant counselling and advice should further be encouraged; and debtors (or even families) should benefit from the partial or total discharge of debts where other measures have not been effective.¹¹²

From the investigation of the European reports and recommendations, stretching over a period of more than 25 years, it is obvious that the European community accepts that insolvency law is necessary where debt becomes too much to bear and should be aligned with the realities of a modern credit society. A striving to achieve a balance between the interests of creditors and insolvent debtors can also be detected, although an earned fresh start for non-fraudulent debtors is preferred to the earlier ultra-liberal application of the fresh start principle in the USA.¹¹³ In this regard, it can be said that the ideals of the European community have coincided with that of the post-BAPCPA model in the USA.

Some more specific preferences that can be deduced from the European recommendations are that specialised courts are preferred and that insolvency procedures should be accessible, simple, quick and inexpensive. Costs and zero redemption capacity should not pose entry barriers. A relatively short period of a maximum of four years seems to be the norm, with certain recommendations favouring a shorter period of three years. Payment obligations should also be reasonable and adjusted to the debtor's needs. Exceptions for taxes, fines and damages are not recommended, although alimony exclusions are provided for. It further seems that informal settlements backed up by some form of cram down are preferred, but that court supervision or the possibility of approaching the courts is

¹¹² *Idem* 3.

¹¹³ See par 2.2.

deemed to be important as it will facilitate informal settlements. The protection of certain assets and income is vital as a decent living standard for the debtor and his family should be ensured. Non-discrimination is another important element and linked thereto is the reduction of the stigmatising effects of bankruptcy. Professional, equipped and independent counselling and legal aid in both out-of-court and court procedures are deemed to be imperative.

2.4 An innovative administrative approach in France

France initiated a novel method, which could possibly lead to a new trend, to reduce the administrative load accompanying insolvency systems without affecting the relief offered to debtors. Leading academics seem to be quite impressed with this development with Kilborn, for instance, observing that¹¹⁴

[o]ver its 20-year lifespan, the French consumer insolvency system has undergone a gradual and impressive evolution toward offering broader and more effective relief to more debtors with less administrative distraction.

It is important at least to consider innovative administrative advancements, especially since reduced administrative functions presumably result in the preservation of resources – a possibility that is especially attractive from a developing country's perspective. The French system and procedures are briefly set out below, not with the intention to do a comparative analysis of the system or even to illustrate the manner in which it provides debt relief, but rather to demonstrate how the system is managed.

In France, the treatment of 'overindebtedness of individuals' starts with a debtor's petition to a regional 'Commission on Individual Overindebtedness' which is primarily administered by the Banque de France – an unlikely player in the field of debt relief.¹¹⁵ Once a petition is received, the commission offers guidance in the development of a debt compromise plan which involves minor concessions (generally referred to as 'ordinary measures') such as interest reductions and the

¹¹⁴ Kilborn 2012 *Loy Consumer L Rev* 24–25. He describes the system with phrases such as 'unique success story', 'spectacular performance shifts' and 'firing on all cylinders'; *idem* 25 and 27. See Kilborn 2005 *Mich J Int'l L* 619 for a thorough description and investigation of the French system pre 2005.

¹¹⁵ The Banque de France is the French central bank. See Kilborn 2005 *Mich J Int'l L* 636–369 as regards the Commission on Individual Overindebtedness.

extension of payment periods.¹¹⁶ As many French debtors only need such mild modifications and the procedure was initially bolstered with the commission's persuasive power (where creditors do not agree to the commission's plan) to make a recommendation to the courts, the majority of cases were dealt with in this 'earliest and least intrusive stage of the process'.¹¹⁷ However, these measures became increasingly inadequate as more consumers struggled to pay their debts due to, amongst others, the economic depression in the early 1990s. Nevertheless, inability to pay was not a basis for the dismissal of a case and the high court expected courts to assist debtors in such 'terminal cases'.¹¹⁸ Therefore, multi-year 'payment plans' deferring all payments were devised. In such instances, debtors regularly lodged repeat filings.¹¹⁹

Reform in 1999 provided for a more effective alternative which resulted in fewer debtors making use of the 'ordinary measures', although more than half of the cases still involve this procedure. The reform entailed a forced discharge in that the commissions could recommend the 'extraordinary measure' of a total deferral of debts for two years,¹²⁰ whereafter the commission would evaluate the debtors position again. If it was found that the 'ordinary measures' of interest deductions et cetera were not viable, the commission could recommend a court-imposed partial or total discharge.¹²¹ Further reform, namely, the 'procedure of personal recovery' followed in 2004. In terms of the latter, the commission may recommend a liquidation of non-exempted assets followed by an immediate discharge, without the need for a repayment plan, in instances where debtors are financially 'irremediably compromised'. This measure largely follows the chapter 7 model in America.¹²²

The cases that did not proceed through the procedure of personal recovery continued to be channelled through the courts 'for an all but automatic judicial

¹¹⁶ Compare the proposed South African pre-liquidation composition procedure; ch 5 par 5.2.

¹¹⁷ For a detailed discussion of the payment plans see Kilborn 2005 *Mich J Int'l L* 639–648.

¹¹⁸ *Idem* 649 n 288 and authorities referred to there.

¹¹⁹ *Idem* 648–649.

¹²⁰ This period was three years and was reduced to two years in 2004.

¹²¹ For a detailed discussion of such 'extraordinary measures' see Kilborn 2005 *Mich J Int'l L* 650–651.

¹²² Kilborn 2012 *Loy Consumer L Rev* 24–26. See par 2.2 as regards the USA system. Also see Kilborn 2005 *Mich J Int'l L* 655–661 for a detailed discussion of this procedure.

imposition of the commission's recommended adjustment plan' until 1 November 2010. On this date two further reforms, which are interesting from a performance point of view, became effective. The first reform does away with the necessity of channelling cases to the courts where 'ordinary measures' are recommended, as the commissions now have the authority to enforce such plans. In this regard, the only remaining form of judicial recourse is an appeal against the imposed 'ordinary measures'.¹²³ The second reform is a simplification of the procedure of personal recovery as very few debtors own any assets of value. A commission can now recommend the procedure without the necessity of a liquidation where 'the debtor possesses only household items that are necessary, of no market value, or the value of which would be "manifestly disproportionate" to the costs of sale.' Although the courts are still involved, they basically rubber stamp such applications, except in opposed matters.¹²⁴ It therefore seems that, in practice, the onus rests on creditors to make out a case as to why the recommendation should not be imposed.

The unorthodox French developments are commended as the jurisdiction found an answer to problems, such as creditor participation and overburdened courts, in an unlikely corner, namely, a central bank that now has a major influence and all but control over the French system. Although unconventional, Kilborn notes that these developments have proved to be one of the most effective features of the French system, as the involvement and support of the central bank were imperative in 'ensuring smooth operation' of the law. Furthermore, the bank lends credibility to the insolvency system from creditors' perspective, which played a major role in the reduction of creditor resistance and the increase in creditor cooperation.¹²⁵ These outcomes naturally have a positive influence on the system's administrative burden.

¹²³ This reform follows the Swedish model. See Maghembe *A proposed discharge* 285–291 for a concise description of the Swedish system and 288–291 as regard the *Kronofogdemyndigheten* or the Royal Debt Collector's Office that is responsible for the bulk of the Swedish system administration.

¹²⁴ Kilborn 2012 *Loy Consumer L Rev* 27–28.

¹²⁵ See Kilborn 2005 *Mich J Int'l L* 638–639.

2.5 INSOL international consumer debt reports

2.5.1 General background

The first set of general principles, attempting to underpin the resolution of consumer¹²⁶ debt problems on an international basis,¹²⁷ was contained in the first *INSOL Consumer debt report* which was published in May 2001 – at the pinnacle of the worldwide economic boom.¹²⁸ Kilborn notes that this report had the advantage of ‘on-the-ground experience’ and legislative material as the 1990s witnessed an explosion of new and modified national natural person debt relief procedures. He also points out that this report served as the foundation of all subsequent major recommendations, including the successive European reports discussed above.¹²⁹ In turn, the report followed the crux of the *Huls Report*.¹³⁰ A second report was published in November 2011 when the world was still trying to digest the impact of the economic downturn.¹³¹ The second edition is mostly an expansion and clarification of the first report,¹³² accompanied by country reports. The principles remained the same, even though the economic climate had changed dramatically in the period in between the two reports. The reports set out four principles and various recommendations under each principle. The first three principles are concerned with the topic of this thesis, namely, remedial measures as regards natural person insolvents. The fourth principle deals with preventative measures and is not considered further.

2.5.2 First principle

The reports insist that consumer debtors who cannot repay their debts are not always to blame for their dire financial situation and that creditors who receive no or

¹²⁶ The reports use the term ‘consumer’ whereas this thesis favours the term ‘natural person’. See ch 1 par 1.6.

¹²⁷ Judge Van Apeldoorn in the foreword to *INSOL Consumer debt report II* states that [t]he objective is to assist the establishment of efficient and effective legal frameworks to address consumer debt problems for national authorities and legislative bodies when preparing new consumer debt laws and regulations or when reviewing the adequacy of existing laws and regulations.

¹²⁸ Kilborn ‘Inaugural lecture’ 4 notes that the report reflects the essence of the *Huls Report*. See Roestoff *in Kritiese evaluasie* 475–481 for a discussion of *INSOL Consumer debt report I* in the 2002 South African context and Roestoff and Renke 2003 *Obiter* 4 *et seq.*

¹²⁹ See par 2.3.

¹³⁰ Kilborn ‘Inaugural lecture’ 4.

¹³¹ See Steyn *Statutory regulation* 402 *et seq* and 2012 *PELJ* 217 *et seq* and Maghembe *A proposed discharge* 55–57 for a discussion of both reports.

¹³² Van Apeldoorn in the foreword to *INSOL Consumer debt report II*.

only minimal payments are not necessarily the victims of the situation.¹³³ The very first INSOL principle is therefore '[f]air and equitable allocation of consumer credit risks'.

Four recommendations and various components or issues to consider under each recommendation are discussed under the first principle, which is the most elaborate and detailed of the four. The first recommendation provides that¹³⁴

[I]n legislators should enact laws to provide for a fair and equitable,¹³⁵ efficient¹³⁶ and cost-effective,¹³⁷ accessible¹³⁸ and transparent¹³⁹ settlement and discharge of consumer and small business debts.¹⁴⁰

Attention should be given to further issues such as the size of the estate,¹⁴¹ the duration of proceedings (which can be seven or eight years),¹⁴² avoiding powers¹⁴³ and an automatic stay of creditor action.¹⁴⁴ The second recommendation provides

¹³³ INSOL *Consumer debt report I* 14 and INSOL *Consumer debt report II* 15.

¹³⁴ INSOL *Consumer debt report I* 14 and INSOL *Consumer debt report II* 16.

¹³⁵ There should be a fair distribution of risk between the debtor and creditors in a predictable and equitable fashion.

¹³⁶ Complex and timewasting procedures should be avoided as consumer debtors usually do not have large estates. It is proposed that the administration of the process should be controlled by capable and efficient trustees or administrators.

¹³⁷ As a fair and equitable procedure is to the benefit of society as a whole, costs should be shared by all stakeholders. The second report mentions that government picks up the bill in many jurisdictions; INSOL *Consumer debt report II* 16.

¹³⁸ No-cost, easy access to the system without several or intricate formalities creating obstacles to such access is preferred. In the event that the system makes provision for bankruptcy and rehabilitation procedures, it is proposed that the consumer should be free to choose between the two.

¹³⁹ Public confidence depends on transparency and therefore debtors and creditors should be able to monitor the process, have the opportunity to be heard, to receive notices and to be able to exercise their rights; INSOL *Consumer debt report I* 15–16 and INSOL *Consumer debt report II* 16–17.

¹⁴⁰ The second report refers to 'debts of a problematic nature'. The debtor should have acted in good faith both as to the way in which the debt arose and the reasons for the inability to repay the debt.

¹⁴¹ It is suggested that the legislator should determine which assets are available for distribution. A proper valuation of assets to be excluded and the redemption capacity should be provided as the debtor should be able to maintain a reasonable standard of living. Special attention should be given to the cost of housing as the high costs thereof may have contributed to the insolvency.

¹⁴² The period referred to is excessive in comparison to European recommendations (see par 2.3) although the reports do not specifically state that they favour such terms. In fact, they provide that proceedings should not be over-extended as consumers may have suffered hardship for quite some time before the procedures were initiated. It will further be unreasonable to expect consumers to live on a limited budget for an extended period of time.

¹⁴³ It should be possible, in line with the principle of equal treatment of creditors, to force creditors to refund transfers received from the debtor within a specific period prior to insolvency procedures.

¹⁴⁴ This will ensure equal treatment amongst creditors; INSOL *Consumer debt report I* 16–17 and INSOL *Consumer debt report II* 17.

that ‘[l]egislators may consider providing for separate proceedings, depending on the specific circumstances of the consumer debtor’.¹⁴⁵ It is proposed that consumers should be free to choose between the procedures and that all procedures should ultimately lead to a discharge and a solution to the core origins of the debt problems. Bankruptcy-type procedures are proposed for estates with low or no redemption capacity and such proceedings could be shorter as there is no benefit in extending them. Rehabilitation procedures, in turn, are better suited to the circumstances of individuals who have relatively larger margins of redemption capacity and may continue for longer periods.¹⁴⁶

The third recommendation provides that ‘[l]egislators should consider providing for separate or alternative proceedings for consumer debtors and small businesses’.¹⁴⁷

The fourth recommendation proposes that¹⁴⁸

[l]egislators should ensure that consumer insolvency laws¹⁴⁹ are mutually recognised in other jurisdictions and should aim at standardization and uniformity.

2.5.3 Second principle

The second principle is the ‘[p]rovision of some form of discharge of indebtedness, rehabilitation or “fresh start” for the debtor’. It highlights the shift from punishment to rehabilitation.¹⁵⁰

Drafters are cautioned against a perception that debt relief procedures provide an easy way out as it will impact on society’s willingness to allow a fresh start. However, the debtor should not be disheartened by entry requirements or alienated from society.¹⁵¹

¹⁴⁵ INSOL *Consumer debt report I* 18 and INSOL *Consumer debt report II* 18.

¹⁴⁶ INSOL *Consumer debt report I* 18–19 and INSOL *Consumer debt report II* 18. The second report mentions that a balance should be struck between earnings and spending as a prerequisite for a discharge.

¹⁴⁷ INSOL *Consumer debt report I* 19 and INSOL *Consumer debt report II* 18.

¹⁴⁸ INSOL *Consumer debt report I* 20 and INSOL *Consumer debt report II* 19.

¹⁴⁹ INSOL *Consumer debt report II* 19 also refers to ‘small business insolvency laws’.

¹⁵⁰ INSOL *Consumer debt report I* 22 and INSOL *Consumer debt report II* 15 and 20.

¹⁵¹ INSOL *Consumer debt report I* 6 and INSOL *Consumer debt report II* 9.

There is only one recommendation under the second principle,¹⁵² namely, that '[l]egislators should offer consumer debtors a discharge of indebtedness as a tailpiece of a liquidation or rehabilitation procedure'.¹⁵³ It draws attention to six distinct issues and recommends that legislatures should take them into account. These issues are contributions to the estate;¹⁵⁴ the extent of the discharge;¹⁵⁵ the waiting period between two discharges; restrictions imposed;¹⁵⁶ anti-abuse provisions;¹⁵⁷ and the possibility of reaffirmation of debt¹⁵⁸ previously discharged.¹⁵⁹

2.5.4 Third principle

The third principle calls for '[e]xtra-judicial rather than judicial proceedings where there are equally effective options available'.¹⁶⁰

In order to effectively assist the debtor, it is proposed that court-driven bankruptcy procedures leading to a discharge should be supplemented by extra-judicial procedures aimed at finding a solution (debt aid) and preventing the debtor from falling into a debt trap again (budgeting aid).¹⁶¹

Where extra-judicial and judicial debt relief procedures are available on essentially the same terms, the extra-judicial procedures offer many more advantages such as flexibility and the saving of time and money. Also, financial difficulties are usually of a non-legal nature and extra-judicial proceedings can be better structured to provide a more integrated approach.¹⁶² Consequently, recommendation six provides that '[l]egislators should encourage extra-judicial or out-of-court proceedings for solving

¹⁵² Recommendation 5.

¹⁵³ *INSOL Consumer debt report I 22* and *INSOL Consumer debt report II 20*.

¹⁵⁴ Post termination income should preferably not be required as a prerequisite for obtaining a discharge.

¹⁵⁵ As many debts as possible should be subject to the discharge as several exclusions may hinder a fresh start.

¹⁵⁶ Restrictions as conditions of a discharge should not obstruct attaining a fresh start.

¹⁵⁷ It is recommended that these provisions should be kept to a limit and be clearly defined. *INSOL Consumer debt report II 21* uses the term 'bad actor provisions'.

¹⁵⁸ This refers to the situation where debtors and creditors agree that certain debts are exempt from the discharge.

¹⁵⁹ *INSOL Consumer debt report I 22–24* and *INSOL Consumer debt report II 20–21*.

¹⁶⁰ *INSOL Consumer debt report I 6–7* and *INSOL Consumer debt report II 10–11*.

¹⁶¹ *INSOL Consumer debt report I 7–8* and *INSOL Consumer debt report II 11* and *22*.

¹⁶² *INSOL Consumer debt report I 25* and *INSOL Consumer debt report II 15* and *22*.

consumer and small business debts problems'.¹⁶³ Creditors should at least receive the same as that to which they would have been entitled under formal procedures and their rights should be protected. The matter should be dealt with in an effective and efficient manner. Debtors should be certain as to which sacrifices are essential in order to obtain a discharge,¹⁶⁴ and that creditors will agree thereto.¹⁶⁵ It is recommended that it should be possible to overrule a dissenting creditor where he would have received materially the same under judicial proceedings and that, in such instances, a court may be required to approve the schemes.¹⁶⁶ It is finally suggested that the cost structure and the need for debtors' representation should be properly considered, as costs should not pose an obstacle to resolving a debtor's financial problems by making use of extra-judicial procedures.¹⁶⁷

Recommendation 7 provides that '[g]overnments, quasi-governmental¹⁶⁸ or private organisations should ensure the availability of sufficient competent and independent debt counselling'.¹⁶⁹ This is because the financial problems experienced by consumer debtors are usually intricate and sometimes more of a socio-psychological than a legal nature. These intermediaries should have expertise in various fields. Provision should also be made for these experts to be trained, financed and supervised. Furthermore, it is suggested that standardised norms, practices and codes of conduct be developed and that the remuneration of intermediaries should be carefully considered to ensure that there is sufficient capacity to properly assist debtors. The reports also caution against unprofessional and dishonest debt counsellors as consumer debtors are usually in a fragile and vulnerable social position which leaves them with no defence against exploitation.¹⁷⁰

¹⁶³ *INSOL Consumer debt report I* 25 and *INSOL Consumer debt report II* 21. *INSOL Consumer debt report II* provides 'for solving consumer and small business debts of a problematic nature.' It is mentioned that in some jurisdictions, formal insolvency procedures coupled with a possible discharge, are not allowed if the consumer debtor cannot attest that an out-of-court settlement could not be reached. The reports suggest that the same result may be obtained by providing for a 'cooling-off' period during which parties should attempt to reach a settlement or agree to a rehabilitation plan.

¹⁶⁴ *INSOL Consumer debt report I* 25 and *INSOL Consumer debt report II* 21.

¹⁶⁵ *INSOL Consumer debt report II* 21.

¹⁶⁶ *INSOL Consumer debt report I* 25–26 and *INSOL Consumer debt report II* 21–22.

¹⁶⁷ *INSOL Consumer debt report I* 26 and *INSOL Consumer debt report II* 22.

¹⁶⁸ The second report uses the term 'semi-governmental'.

¹⁶⁹ *INSOL Consumer debt report I* 26 and *INSOL Consumer debt report II* 22.

¹⁷⁰ *INSOL Consumer debt report I* 27 and *INSOL Consumer debt report II* 22.

2.5.5 Recommendations to stakeholders

In summary, INSOL proposes specific steps or action plans to be taken by stakeholders. Recommendations relating to legislatures are as follows:¹⁷¹

- (a) Enact laws to provide for a fair and equitable, efficient and cost effective, accessible and transparent settlement and discharge of consumer and small business debts.¹⁷²
- (b) Allow partial or total discharge of the debts of individuals and, where applicable, families in cases of over-indebtedness where other measures have proved to be ineffective, with a view to providing them with a new opportunity for engaging in economic and social activities.¹⁷³
- (c) Provide for appropriate alternative proceedings depending on the circumstances of the consumer debtor.¹⁷⁴
- (d) Consider providing for more appropriate separate or alternative proceedings for consumer debtors.¹⁷⁵
- (e) Ensure that consumer debtor insolvency laws are mutually recognised in other jurisdictions and aim at standardization and uniformity.¹⁷⁶
- (f) Offer the consumer debtor a discharge from indebtedness as a method of concluding a bankruptcy or rehabilitation procedure.¹⁷⁷
- (g) Effectively limit the means of creditors to hinder debt settlements unreasonably.¹⁷⁸
- (h) Ensure that payment plans in debt adjustment are reasonable, in accordance with national practices, both in repayment obligations and in duration; ensuring that debt adjustment covers all debts, excluding only those covered by special waivers provided under national law.¹⁷⁹
- (i) Encourage the development of extra-judicial or out-of-court proceedings in order to resolve the problems of consumer debts.¹⁸⁰
- (j) Establish mechanisms for extra-judicial settlements and encouraging such settlements between the debtor and creditor.¹⁸¹

Governments, semi-governmental or private organisations are encouraged to:¹⁸²

- (a) Ensure the availability of accessible, sufficient, competent and independent pre and post bankruptcy debt-counselling.
- (b) Set up voluntary educational programmes to improve information and advice on the risks attached to consumer credits.
- (c) Encourage the development of extra-judicial or out-of-court proceedings in order to resolve the problems of consumer debts.

¹⁷¹ INSOL *Consumer debt report I* 11 and INSOL *Consumer debt report II* 13.

¹⁷² *Ibid.*

¹⁷³ INSOL *Consumer debt report II* 13.

¹⁷⁴ INSOL *Consumer debt report I* 11 and INSOL *Consumer debt report II* 13.

¹⁷⁵ *Ibid.*

¹⁷⁶ INSOL *Consumer debt report I* 12 and INSOL *Consumer debt report II* 13.

¹⁷⁷ *Ibid.*

¹⁷⁸ INSOL *Consumer debt report II* 13.

¹⁷⁹ *Ibid.*

¹⁸⁰ INSOL *Consumer debt report I* 12.

¹⁸¹ INSOL *Consumer debt report II* 13.

¹⁸² INSOL *Consumer debt report I* 12 and INSOL *Consumer debt report II* 13–14.

- (d) Set up policies relating to debt management and to treatment of over-indebted individuals and families and ensuring uniformity of such policies.
- (e) Collect information and statistics on debt problems and analyse the situation of over-indebted individuals and families in their countries.
- (f) Encourage effective financial and social inclusion of over-indebted individuals and families, in particular by promoting their access to the labour market.
- (g) Encourage the active participation of the debtor in debt settlement and, where necessary, counselling and advice following the debt settlement.
- (h) Set up debt advice, counselling and mediation mechanisms, as well as ensuring, or at least encouraging, effective participation of lending institutions and other public and private creditors in implementing national policies for debt management.
- (i) Ensure appropriate quality standards and impartiality of the services provided by the responsible bodies and professionals as well as effective mechanisms for controlling these standards.¹⁸³

2.5.6 Synopsis

An interesting fact that emerges from both of the INSOL reports is that the principles were not amended between 2001 and 2011, despite drastic fluctuations in the economic environment during that period. The fact that experts in the field still accepted the original principles in an economically volatile climate underlines their credibility.

In line with the European recommendations¹⁸⁴ and perhaps also with the approach presently followed in the USA,¹⁸⁵ a balanced approach is proposed in that consumer credit risks should be fairly and equitably allocated. Legislatures are encouraged to enact laws providing for accessible, efficient, cost-effective settlement and discharge procedures which are also favoured in the European community. Another similar recommendation is that the duration of proceedings should not be over-extended.¹⁸⁶ No preference as regards the maximum term is expressed, although periods of up to eight years are mentioned. The reports do not deal with specialised courts and how to deal with consumers who do not have redemption capacity. However, it is recommended that separate proceedings, depending on the specific circumstances

¹⁸³ Recommendations (c)–(i) only appear in INSOL *Consumer debt report II*.

¹⁸⁴ See par 2.3.

¹⁸⁵ See par 2.2.

¹⁸⁶ See par 2.3.

of the debtor, should be devised and that the debtor should be free to choose between them.

Emphasis is placed on the fresh-start principle as is the case in the USA and is recommended in Europe.¹⁸⁷ As it is cautioned that the procedures should not be regarded as an easy way out, it seems that the European *earned* fresh start is favoured,¹⁸⁸ although it is warned that the debtor should not be disheartened or socially excluded. The discharge should be as wide as possible and it is suggested that restrictions and anti-abuse provisions be kept to a minimum.

Similar to the European endorsements,¹⁸⁹ extra-judicial proceedings are favoured as they are flexible, save costs and time and can be better structured according to the debtor's financial difficulties which are usually non-legal in nature, although judicial proceedings should also be available. It is recommended that extra-judicial proceedings should be available on essentially the same terms as judicial proceedings and that it should be possible to overrule a dissenting creditor where he would have received the same in terms of judicial proceedings. In the latter instance, the court may be required to approve such plans. It is specifically recommended that expert and professional debt counselling should play a role in extra-judicial proceedings. As was gathered from the European position,¹⁹⁰ it is suggested that costs may have to be shared by all stakeholders.

2.6 World Bank Report on treatment of the insolvency of natural persons

2.6.1 General background

In January 2011, the World Bank convened its Insolvency and Creditor/Debtor Regimes Task Force¹⁹¹ to discuss revisions to the ICR Standard and a number of insolvency-related issues that came to the fore in the midst of the global financial crisis. The Task Force was mandated to consider the issue of natural person

¹⁸⁷ See par 2.2 and 2.3.

¹⁸⁸ See par 2.3.

¹⁸⁹ *Ibid.*

¹⁹⁰ See par 2.3.

¹⁹¹ Hereafter the 'Task Force'.

insolvency for the very first time. The World Bank and the Task Force created a special working group to study natural person insolvency and to produce a reflective report, suggesting guidance whilst keeping the diverging policy options and sensitivities around the world in mind.¹⁹² The final report, titled *Report on the treatment of the insolvency of natural persons*, was published in December 2012. It is non-prescriptive¹⁹³ and frames its objective in the following terms:¹⁹⁴

[T]o provide guidance on the characteristics of an insolvency regime for natural persons and on the opportunities and challenges encountered in the development of an effective regime for the treatment of the insolvency of natural persons.

Before turning to the actual attributes of effective insolvency systems, the report sets off with a lengthy introduction, which paves the way for further discussions. Here it is emphasised that the report focuses on the treatment of insolvency, not on the prevention thereof or on poverty *per se*.¹⁹⁵ It further does not attempt to distinguish between ‘pure’ consumers and those engaged in business as it concentrates on shared core issues relevant to natural person debtors alike, whether or not they are engaged in business – which is also the approach followed in this thesis.¹⁹⁶ Some pertinent preliminary comments revolve around the fact that insolvency regimes must take cognisance of the adjacent environment of laws, policies and practices.¹⁹⁷ In this regard, countries are urged not to adopt a ‘mainstream approach’, but rather to take into account the broad range of purposes to be served and the degree to which they are relevant to a jurisdiction’s unique circumstances.¹⁹⁸ However, the importance of an insolvency system is emphasised by, amongst others, listing its many benefits to debtors,¹⁹⁹ creditors and most importantly (it seems) society.²⁰⁰ In

¹⁹² WB *Report* 1–3.

¹⁹³ *Idem* 4–5 and 128.

¹⁹⁴ *Idem* 3–4 and 125.

¹⁹⁵ *Idem* 10–13. In South Africa, insolvency of natural persons and poverty more often than not overlap; see ch 1 par 1.1.

¹⁹⁶ WB *Report* 13–16. See also ch 1 par 1.6. The ICR Standard, in contrast, concentrates on business insolvency.

¹⁹⁷ WB *Report* 7–9 and 126.

¹⁹⁸ *Idem* 18–19. However, see Spooner 2013 *ERPL* 788 and 2012 *Am Bankr LJ* 243 where he suggests that national factors should not be over-emphasised.

¹⁹⁹ Benefit to debtors is contrary to the South African position where benefits to creditors take centre stage; see Boraine and Roestoff 2014 *THRHR* 533 and ch 1 par 1.1.

²⁰⁰ WB *Report* 19–40 and 126. See also Boraine and Roestoff 2014 *THRHR* 533 and Kilborn 2014 *PILR* 3. The report groups benefits to society into two categories; WB *Report* 27. In this regard it provides as follows:

Footnote continues on next page

order to attain these benefits, insolvency systems strive to improve the adverse systemic effects of unregulated distressed debt.²⁰¹

Although the introduction of insolvency systems is regarded as important, the report is realistic in recognising significant concerns when considering the adoption of such a system for natural persons. These concerns are categorised as debtors' moral hazard,²⁰² fraud and stigma. Nevertheless, many systems have overcome these concerns which need not stand in the way of the numerous benefits that insolvency procedures for natural persons have to offer.²⁰³ Some solutions are offered and as regards moral hazard, it is suggested that the most sensible approach is to design and implement proper access requirements for both entry into the insolvency system and the discharge therefrom. However, a balance should be struck so that access is not unduly restricted as this will negate the benefits of the system.²⁰⁴ In any event, little evidence of moral hazard has surfaced in even the most liberal of systems.²⁰⁵ Debtors' fraud²⁰⁶ can in turn be addressed through cautious monitoring by administrators and creditors.²⁰⁷ Stigma²⁰⁸ is considered an especially difficult challenge due to, amongst others, cultural perceptions. Public campaigning regarding education and awareness; the avoidance or reduction of judgmental language, punitive measures, civil disabilities and post-relief restrictions in

One category encompasses a variety of benefits associated with disciplining creditors to acknowledge the reality of their low-value claims against distressed debtors, internalize the costs of their own lax credit evaluation, and more effectively and fairly redistribute those costs among the society that benefits from the availability of credit. The other category focuses on the *intra*-national and *inter*-national benefits of maximizing engagement and productivity by debtors, especially in light of the increasingly competitive global marketplace.

²⁰¹ *WB Report* 27 and 126–127.

²⁰² Some policymakers express concern that 'improper incentives' to escape debt will create moral hazard in that debtors will be motivated to act immorally or irresponsibly by taking up more credit than they can service and thereafter negating their responsibilities once insolvency has materialised; *idem* 40.

²⁰³ *Idem* 40–44 and 127–128. See also Boraine and Roestoff 2014 *THRHR* 533–534.

²⁰⁴ *WB Report* 41. It is mentioned that policy makers have in recent years increasingly considered the benefits that an insolvency system has on reducing *creditors'* moral hazard, namely, balancing the wish for maximum profitability with the need of cautious underwriting and assessment of a debtor's ability to pay; *ibid.*

²⁰⁵ *Idem* 64.

²⁰⁶ This issue is closely linked to moral hazard in that some policymakers believe that debtors would unduly gain access to the system and its extraordinary benefits by means of fraud. Manners in which such fraud can occur are for example the concealment of assets or income or the truth about the debtor's financial situation; *idem* 42.

²⁰⁷ *Idem* 42.

²⁰⁸ The concern in this regard is that honest but unfortunate debtors are avoiding the system due to its stigmatising effect; *idem* 43.

legislation; discharge; and property exemptions are mentioned as possible deterrents.²⁰⁹

2.6.2 Core legal attributes of an insolvency regime for natural persons

The report discusses six broad matters under the heading ‘core legal attributes’. These are general system design; the institutional framework; access to the system; creditor participation; procedural solutions and the payment of claims; and discharge.

2.6.2.1 General system design

There are two important preliminary issues as regards the general system design. The first deals with the interaction between the formal system and the generally favoured informal, negotiated alternatives.²¹⁰ The second deals with the question where a formal system should be located.²¹¹

As far as informal alternatives are concerned, it is noted that it offers many (theoretical) advantages, for instance reduced stigma, lower costs and increased flexibility.²¹² However, in contrast with earlier studies,²¹³ the report expresses little confidence in settlement procedures and states that their merits are often illusory. Some of the reasons for the scepticism are that it is difficult to reach agreement with all creditors and that informal procedures are usually plagued by delays. There is a further risk of creditors pressuring debtors to enter into non-viable plans. It is proposed that the probability of success may be improved by rendering voluntary settlements binding on the minority and passive creditors, although it is stated that the rights of dissenting creditors should be regulated. Furthermore, institutional support and incentives are needed. In countries where such systems are most successful one of two elements can generally be detected – either negotiations are overseen or facilitated by a persuasive government regulator or a central, well-established counselling agency has established productive relationships with creditors. It is mentioned that the assistance must be professional and low or cost

²⁰⁹ *Idem* 43–44 and 128.

²¹⁰ *Idem* 45–49. See also Boraïne and Roestoff 2014 *THRHR* 534–535.

²¹¹ *WB Report* 49–52. See also Boraïne and Roestoff 2014 *THRHR* 535–536.

²¹² See *WB Report* 45–46 and 129 as regards the advantages of negotiated settlements.

²¹³ See for instance the European approach; par 2.3. See also Kilborn 2014 *PILR* 5 where he notes the departure from former recommendations.

free. Furthermore, negotiations should take place without an immediate threat of enforcement. Nevertheless, even if these proposals are built in, only those who experience mild or temporary financial difficulty are likely to succeed in informal negotiations.²¹⁴

The second preliminary issue deals with the placement of formal insolvency procedures. In this regard, it is mentioned that the role of the judiciary needs to be established. It is stated that fundamental insolvency law and associated issues all relate to the rights of creditors and debtors, which are ultimately adjudicated and enforced by the judiciary. Furthermore, recourse to the courts is a human rights issue. Some court involvement is therefore to be expected, both as a result of the traditional law of obligations and constitutional and human rights policies. However, the desired degree of court involvement should be considered.²¹⁵ Another matter relating to the placement of the legislative scheme is whether personal insolvency should be contained in a specific piece of legislation or whether it should form part of general insolvency law, as both options have merit.²¹⁶ On the one hand, a separate piece of legislation creates a better opportunity to take cognisance of the special needs of insolvent individuals – especially where broader counselling is needed. On the other hand, a separate piece of legislation is generally designed for relatively simple cases. However, some natural person insolvency matters involve complicated legal issues, for instance where natural persons have a background of business failure. In these instances a general insolvency law is more appropriate.²¹⁷

²¹⁴ *WB Report* 48–49 and 130.

²¹⁵ *Idem* 49–50 and 130.

²¹⁶ *Idem* 50. Natural person insolvency in Anglo-American systems has generally developed as part of general insolvency law. It is said that these procedures are usually a summary and simplification of business insolvency procedures. Other countries choose to deal with personal insolvency in a separate piece of legislation, some of these laws being specifically structured to serve persons not involved in substantial business activity; *idem* 51.

²¹⁷ *Idem* 51. See the South African 2015 Insolvency Bill that attempts to combine insolvency procedures for both juristic and natural persons in one piece of legislation. At present these fields are regulated by separate laws; ch 1 par 1.1.

2.6.2.2 *Institutional framework*

The second broad issue contemplated under core legal attributes of an insolvency regime for natural persons is the institutional framework.²¹⁸ Six specific matters are discussed under this heading, the first being the classification of existing systems. Here it is explained that institutional frameworks can range from

- (1) systems in which an administrative agency dominates;²¹⁹ to
- (2) hybrid public/private systems where public processing of insolvents co-exists with private restructuring alternatives; and to
- (3) court-based systems primarily serviced by publicly funded or private intermediaries.

Systems can thus be classified in accordance with the role that the private and public sectors have to play. In this regard a balance is proposed as too much emphasis on any of the sectors may have negative consequences.²²⁰

Secondly, '[c]ourt-based systems and the role of courts' are discussed, although some references have been made to this aspect before. While the majority of jurisdictions still rely on court-based systems, their role may vary and there is an increased tendency to limit the role of courts in high-income jurisdictions. It seems that the report acknowledges that courts have an important role to play, but prefers the situation where their intervention is the exception rather than the rule. Some institutional advantages of court involvement are noted. These are that presiding officers are generally viewed as impartial and trustworthy and that constitutional and human rights norms may require court involvement. Courts can further oversee intermediaries and address disputes that may arise. However, many disadvantages of systems that rely heavily on the courts are mentioned. These are, amongst others, high costs; delays; pressure on public funding; variable decision making by presiding officers; the limited ability of lower courts to address debt-related issues; and perceptions that courts are unapproachable and intimidating and that they focus on legal rights where individual insolvency cases are primarily viewed as administrative

²¹⁸ See *WB Principles* pts C and D as regards legal, institutional and regulatory frameworks in business insolvency.

²¹⁹ See for instance the French system; par 2.4.

²²⁰ A large private sector is susceptible to the abuse of debtors, which may result in costly public regulation. There is further a belief that debt problems are social in nature and can only be addressed by the courts. However, the private sector does offer many benefits, not least in skills, and a system solely rooted in the public sector is likely to experience delays; *WB Report* 55 and 130.

in nature. Where courts are involved it is noted that the training of presiding officers is important.²²¹ It is suggested that²²²

[t]he pressure on public funding of the judicial system, the limited ability of lower courts to address economic and social issues of debt, and variable decision making by judges create pressure for increased specialization and administrative processing particularly for the large percentage of ‘NINA (no income, no assets) debtors’, and more effective sorting of cases where private negotiation will be meaningful.

Next, ‘[t]he role of trusted intermediaries’ is discussed and described as vital in establishing a reliable and sustainable system. It is acknowledged that intermediaries often have potentially conflicting roles to play and that, in a multi-track system, significant power is entrusted to them. This may result in intermediaries furthering their own financial or ideological interests. Simplification is yet again offered as a possible solution. Cost constraints are also mentioned and in this regard properly designed computer programmes are proposed as they can reduce the need for professional discretion and may assist in channelling consumers to different solutions, which may attain long-term social benefits. It is mentioned that strong ethical codes and/or regulation are necessary, but that a balance should be attained between ensuring intermediaries are qualified to address the problems of insolvents and prohibiting undue restriction on individuals who may offer advice and assistance.²²³

In the fourth place, ‘[a]dministrative models of insolvency processing’ are considered. It is recognised that public agencies play significant roles in the sorting, processing and administration of cases in several countries, which have many benefits but also disadvantages.²²⁴ In order to negate some disadvantages, it is suggested that the possibility of a conflict of interest be addressed by separating administrative and investigating functions; adopting clear measures of success to ensure appropriate monitoring and reporting; and retraining staff (where existing institutions are built

²²¹ *Idem* 55–56.

²²² *Idem* 56.

²²³ *Idem* 57–58.

²²⁴ The benefits include that administrative processing can provide a steady bureaucracy and develop skill in identifying and sorting cases. It can also offer independent advice and information, deter abuse and address moral hazard issues. However, there are disadvantages, namely, the danger of capture and potential conflicts of interest.

upon).²²⁵ A remark which is important in the context of this thesis is that state processing of insolvent debtors who do not have sufficient means to cover the procedural costs raises funding issues.²²⁶

A discussion of '[c]omparative institutional issues in the choice of the institutional framework' follows and it is noted that a comparative analysis of the role of courts and administrative agencies must consider the context of existing institutions, especially since developing economies may face significant costs in establishing novel nationwide infrastructures. Furthermore, legal transplants of complex procedures onto poorer countries should be avoided as courts may not have the capacity to deal with the demands of these procedures. It is suggested that existing institutional infrastructures should rather be expanded and that procedures should be simplified. Incremental changes, when necessary, may prove to be more politically acceptable. It is again noted that computer technology can reduce processing and error costs. Online access via approved intermediaries (using standardised programmes) coupled with possible random audits and utilising data from credit bureaux could provide relief and prevent abuse.²²⁷

'Financing issues' constitute the final consideration as regards the institutional framework.²²⁸ Because insolvency systems offer economic and social benefits to all role-players, it is suggested that debtors, creditors and society at large should contribute their 'fair share'.²²⁹ The report mentions that financing issues can be softened by addressing expenses and therefore proposes the introduction of

²²⁵ WB Report 58–60.

²²⁶ *Idem* 60.

²²⁷ *Idem* 60–61 and 131.

²²⁸ The report notes five approaches to financing. These are:

- (1) state funding of the process (including both creditor and debtor costs);
- (2) cross-subsidization of low value insolvencies by higher value estates;
- (3) state subsidies to professionals involved in the process and writing off court costs where there is an inability to repay;
- (4) levies on creditors, such as taxation of distressed debt to fund those cases where individuals have no ability to pay; and
- (5) no state support beyond any general public good funding of the court system.

It is mentioned that the last option is most common; *idem* 61.

²²⁹ This may according to the report, *idem* 62, mean that creditors contribute through a levy. Creditors may pass along some of this cost to the public, but may also have incentives to reduce the number of debtors in default. For some debtors with limited resources fair share could mean no contribution.

summary procedures, which only require compliance with traditional formalities in exceptional circumstances, and the improved use of online systems.²³⁰

2.6.2.3 Access to the formal insolvency system

‘Access to the formal insolvency regime’ is the third matter dealt with under ‘Core legal attributes’. Apart from some introductory remarks, ‘[d]ebtor access’ and ‘[c]ontrolling access in a multi-track system’ are specifically considered. It is noted that access ought to be transparent and certain and that access requirements should safeguard against improper use by both creditors and debtors. In jurisdictions where creditors are allowed to file insolvency procedures, it can be misused and should therefore be regulated. The two traditional entry standards of access to insolvency, namely, the ‘cessation of payments test’ or the liquidity test²³¹ and the balance sheet test, are mentioned.²³² The former is generally preferred in natural person insolvency and is easier to apply. ‘Acts of bankruptcy’ are said to be out-dated, as the focus is on the inability to pay and not on the wrongful actions of the debtor.²³³

As far as ‘debtor access’ is concerned, it is stated that complicated access requirements may keep debtors in a state of informal insolvency, where they lose incentives to participate in society, may rely on state support and even disappear to hide from creditors. On the other hand, systems with lower access barriers have the benefit of reducing honest but unfortunate debtors’ reluctance to seek relief. However, such systems may require good behaviour as a requirement for a discharge. Creditors or state agencies may play a role in challenging the discharge, which protects against moral hazard and, through increased participation, improves the legitimacy of the system. Nevertheless, criteria for challenges should be clear as benefits may be overshadowed by increased decision making and error costs. Conferring substantial discretion on presiding officers to decide on discharge issues is not favoured as it results in variation in decision making and it is difficult to judge behaviour in hindsight.²³⁴

²³⁰ *Idem* 61–62 and 131. See also Boraine and Roestoff 2014 *THRHR* 536.

²³¹ This test measures whether a debtor is able to pay debts as they mature.

²³² This test measures whether a debtor’s fairly valued liabilities exceed his fairly valued assets or the other way around. See UNCITRAL *Guide* 45–47 and WB *Principles* C4.2.

²³³ WB *Report* 62–63.

²³⁴ *Idem* 63–66 and 132.

Returning to the discussion of debtor access to procedures, it is noted that in many jurisdictions, insolvency has to be proved.²³⁵ Insolvency does not necessarily have the same technical meaning in all jurisdictions as it can be defined as ‘a current inability to meet present debts’ or may include ‘the possibility of debtors being able to improve their financial situation and repay debts at a future date’. The ‘permanent insolvency’ perspective is regarded as speculative and uncertain. This also results in the need for increased decision making and error costs.²³⁶

It is mentioned that, in an attempt to reduce debtors’ moral hazard, some access barriers may be devised to ‘ensure’ that agreements are kept. In line with previous comments on moral hazard, it is stated that such restricted approaches are expensive and open access countries in any event show little evidence of moral hazard. It is further not necessary to curb access as sanctions may be imposed after entry. Moral hazard can further be addressed by limiting the frequency of access to the system or to subject repeat insolvents to more intensive investigation. As the ‘good faith’ requirement represents many problems, for instance difficulties in judging conduct in hindsight, most systems have a lower standard of intentional fraud or the concept of honesty. Some jurisdictions prescribe consultation with intermediaries to curb abuse of the system. However, evidence shows that compulsory counselling is drastically over-inclusive in defending against abuse or in assisting debtors to avoid insolvency.²³⁷ A blanket requirement may further channel limited resources away from matters where such interventions will be most productive.²³⁸

Finally, the report suggests that debtor access may be determined by making use of a combination of rules and standards. The preferred position seems primarily to make use of rules and couple such with limited discretion, as such an approach will be less costly to administer and will reduce the need for advanced expertise. The

²³⁵ Open access systems’ only entry requirement is that individuals must meet an insolvency test; *idem* 63.

²³⁶ *Idem* 64.

²³⁷ This is contrary to the INSOL reports that are in favour of debt counselling; par 2.5.

²³⁸ WB Report 64–66 and 131.

report consequently favours the position where legislatures draft clear rules and avoid passing responsibility to the courts through a certain standard.²³⁹

The second specific issue regarding access in general relates to '[c]ontrolling access in a multi-track insolvency system'. Here the issue is whether access should be reliant on consumer choice or a decision should be taken by a public agency or official. In this regard, costs involved and the role of intermediaries are affected by the decision. Where consumer choice is favoured, intermediaries are necessary to assist debtors in decision making and there should be mechanisms in place so that creditors or public agencies can monitor and challenge these decisions. Furthermore, intermediaries may have considerable power which poses the danger that they may steer debtors in accordance with their own financial or ideological interests. This calls for regulation. It is suggested that simplification can minimise such power and has the added benefit of reducing debtors' information costs and information processing costs. Where public agency decision making is preferred, disinterested choices are made which ensure integrity and reduce costs. However, the report suggests that measures should be in place to ensure consistent treatment and enable challenges to decisions.²⁴⁰

2.6.2.4 Creditor participation

The '[p]articipation of creditors' is the fourth point of discussion. It is observed that, in general, natural person insolvency rarely yields notable value and that creditors therefore usually remain passive. Some jurisdictions have dealt with the issue by lowering creditor quorums. However, the most common approach is the limitation (or even exclusion) of creditors' participation – except in instances where the estate represents significant value. A trend has consequently developed, as a matter of

²³⁹ *Idem* 65 and 131. See also Boraine and Roestoff 2014 *THRHR* 537 n253 where they refer to the South African position as regards sequestration proceedings, where the judiciary is responsible for managing access through a standard, namely, the advantage for creditors' requirement. See further ch 1 par 1.1.

²⁴⁰ *WB Report* 67–68 and 132. The report also observes that in certain systems access is dependent on prior consultation with intermediaries with the objective of obtaining advice as to the different alternatives. Other systems use initial screening to determine debtor's choice. A further access criterion is that access is only provided to those with consumer debts, which is not regarded as the optimal approach as such exclusions may result in litigation over the nature of debts and increase screening costs. It may further deny access to those with business debts although their factual situations may be similar to those with only 'consumer debt'; *idem* 68 and 132.

course, to do away with creditor participation and to allow it only in extraordinary circumstances.²⁴¹

As regards creditor participation in plan confirmation, creditors generally have slight or no significant influence over the establishment of a payment plan or other requirement for discharge or relief. This is because of the moral and economic emphasis on salvaging and preserving natural persons and their families. Once a natural person seeks formal insolvency relief, natural market forces and free contract negotiation are usually no longer efficient safeguards of public health and welfare. Another reason why creditor participation is limited is that creditors' rights are protected through their representation by public authorities who are better suited to decide on complex issues such as levels of sacrifice and compromise. Other ways in which creditors' rights are guaranteed are for instance the opportunity to be heard in a court or an administrative procedure. Furthermore, the law may provide for the reopening of a case where assets or unexpected income are discovered post-discharge or post-confirmation. In such instances, the discovered value will be collected and retroactively distributed to creditors. However, such windfalls are usually not available to creditors and finality may be considered as more important than ensuring maximal payment to creditors. It is clear that the report favours the position where decision making on payment plans and discharge are left to the courts or administrative bodies.²⁴² Creditors' participation in '[c]laims submission and verification' is also specifically considered and it is noted that such participation is at present a rare phenomenon except, once again, in instances where the administrator found value for distribution. Where claim filings are retained, many countries sanction incorrect or fraudulent claims.²⁴³

2.6.2.5 Procedural solutions and payment of claims

'Solutions to the insolvency process and payment of claims' are the fifth issue considered in the report. It also represents the most involved discussions and deals with payment by means of liquidation of the estate and through a repayment plan. Next, the advantages and disadvantages of the two different approaches to payment

²⁴¹ *Idem* 68–69 and 132.

²⁴² *WB Report* 69–73 and 132–133.

²⁴³ *Idem* 73 and 133.

are addressed. Special consideration is given to the payment of secured loans, including mortgages. A pertinent theme running through all of these discussions is that, although maximising creditors' return continues to play a significant role in insolvency, experience has shown that there are many complications when attempting to extract value from natural persons.²⁴⁴

'Payment through liquidation of the estate' is dealt with under the subheadings 'property exemptions', 'specific exemptions by asset type', 'the consequences of the exemption regime', 'after-acquired property' and 'family property and division of assets'.²⁴⁵ Some initial comments are that, although most modern systems continue to concentrate on assets, it is only a formality as the vast majority of debtors do not have assets of value. In line with this reality only assets of considerable value are generally liquidated as substantial administrative expenses are only allowed in such instances. Furthermore, most contemporary societies have decided that debtors cannot be left without assets to support themselves and their families. Property exemptions are therefore closely related to the discharge principle and sometimes to exemption policies in non-bankruptcy law.²⁴⁶

As regards 'property exemptions' the report notes that exempt property was historically set at very low levels – an unforgiving approach derived from a culture where creditors were sceptical of debtors' *bona fides*. As such attitudes are outdated, a growing trend to liberalise exemptions has developed. However, the general principle that exemptions do not affect security interests is emphasised.²⁴⁷ Three different approaches to property exemptions can be detected. The first is the exemption of a narrow range of assets up to a certain value.²⁴⁸ Where the levels and scope of exemptions are not increased, they become ignored in practice. The second approach is a modern version of the first where provision is made for a broad

²⁴⁴ *Idem* 133.

²⁴⁵ See Evans *A critical analysis* ch 9 as regards property excluded or exempted from the insolvent estate in South Africa. See also ch 3 of this thesis for a discussion of the South African approach.

²⁴⁶ *WB Report* 74 and 133. See also Boraine and Roestoff 2014 *THRHR* 538.

²⁴⁷ As regards the importance of immovable and movable property as security for debt in modern economies, see *WB Principles* A2, A3 and A5.2.

²⁴⁸ Historically, these assets were limited to very low monetary levels, which dates back to an era where insolvency law was penal in nature and where debtors and their families lived close to poverty.

range of categories up to a certain amount. The debtor bears the burden to establish an exemption of these assets. This approach stems from the notion to protect debtors from post-judgment execution against assets and is followed in many jurisdictions. The second approach is said to have the advantage that it is mostly fair and may work well in countries where insolvents generally come from the middle class and have several assets. However, it is noted that fairness comes at the expense of efficiency as there may be disagreement where a debtor attempts to maximise benefits. The report tables a further weakness in that, where the limits on value are too low or become out-dated, they are not adhered to in practice. This results in debtors retaining more than what they are entitled to. The third approach is a more general standards-based approach that exempts most property from the estate and confers the obligation to claim assets of excess value on the insolvency representative. A fundamental theory of this approach is that the assets are much more valuable to the debtor than what the actual economic value thereof represents. In jurisdictions where most insolvent debtors have limited personal assets²⁴⁹ this approach may prove to be most efficient.²⁵⁰

The exemptions that systems allow for can also be examined in terms of the assets that are covered. The first specific exemption that the report deals with is, not surprisingly, the family home, which represents the most important asset of the debtor and his family. It is also the asset in which debtors usually have lost the most equity. Although there is general agreement as to the importance of this exemption, there are various approaches to and limitations on the protection it provides. This ranges from no limit as to the monetary value to a mere right to reside in the home for a specific period of time.²⁵¹

The second important exemption considered by the report involves automobiles or modes of transportation. Depending on the circumstances of the debtor, these assets could be directly linked to the retention of employment. The exemption of professional books, implements, equipment or tools of trade is another issue for

²⁴⁹ South Africa constitutes such a jurisdiction; ch 1 par 1.1.

²⁵⁰ *WB Report* 74–78 and 133–134.

²⁵¹ *Idem* 79. For the South African position regarding the treatment of the home in insolvency law, see *Steyn Statutory regulation* ch 6.

consideration. The report submits that it is logical that higher limitations should be established in line with the increased focus on debtor rehabilitation. Furthermore, in many jurisdictions, the tools of trade exemption is linked to the automobile exemption. Household furnishings are listed as a further common exemption as in most instances the value thereof is very low. Also, most systems exempt debtors' post-commencement salary or wage, although some systems require or encourage debtors to pay a portion thereof to the estate. In the latter instance, the minimum amount to be retained should at least cover reasonable domestic needs. The retention of pension or retirement funds is said to be one of the most important exemptions to consider as these funds usually represent the debtor's largest asset. However, this issue is extremely complex and requires careful and specific attention.²⁵²

It is said that the 'consequences of the exemption regime' are far reaching and that the modern trend to enable debtors to start afresh should be observed. The debate is thus concerned with the level of sufficiency. The cost of administration and the efficiency thereof should further be taken into account when deciding on a specific approach, as these factors vary significantly depending on the chosen regime. In this regard an important factor in system design is the efficient use of resources when liquidating low-value assets.²⁵³

Even though 'after-acquired property' is generally not available for distribution amongst creditors, the absence of regulation in this regard could result in debtors strategically filing insolvency petitions to retain post-petition windfalls. Therefore, many jurisdictions prescribe that certain post-petition or post-insolvency order interests, acquired within a specified period, are available for distribution.²⁵⁴

The issue of 'family property and division of assets' is the last consideration under the liquidation procedure. It is said that in general, joint ownership results in complicated legal issues and that the answer thereto is usually found in non-insolvency law. The report consequently warns that such issues are even more

²⁵² WB Report 79–82.

²⁵³ *Idem* 82 and 134.

²⁵⁴ *Idem* 82–83.

complex where they involve the family home, where co-owners are spouses and where there is no substantial financial benefit to creditors.²⁵⁵

‘Payment through a payment plan’ is discussed next. Since debtors in financial distress rarely have valuable assets, systems generally provide for a contribution from future income in exchange for the benefits that an insolvency system offers. It can therefore be said that most systems prescribe to an ‘earned start’ rather than a ‘fresh start’.²⁵⁶ Formulating a payment plan is a difficult process, especially as regards the issues of ‘plan duration’ and ‘payments to creditors’. Further considerations are ‘plan implementation, monitoring and supervision’ and ‘modification of payment plans for changes in debtor’s circumstances’.²⁵⁷

Plan duration, at least in part, relies heavily on the goals of the plan. If the goal is to maximise payment to creditors, it may at first seem obvious that a longer period would be more appropriate. However, longer terms contradict several of the primary goals of natural person insolvency systems which, amongst others, harbour the idea of removing disincentives to increase productivity. The report therefore cautions that longer plans can, contrary to the intention with which they were created, reduce debtors’ motivation and consequently their productivity, which have an effect on creditors’ return. Experience has further shown that few debtors have anything, beyond basic living expenses and administration costs, to offer creditors, irrespective of the length of the repayment period. It is therefore submitted that longer periods are more likely to weaken returns and decrease the number of debtors assisted, thus limiting the positive effects of the system. A more attainable goal (of payment plans) seems to be the financial education of debtors.²⁵⁸

As regards the determination of the actual term, two techniques can be detected. The first is to leave period determination to the discretion of a decision-maker on a case-to-case basis. The second is to include a single standard in legislation. It is mentioned that the first flexible approach has led to unwanted and self-defeating

²⁵⁵ *Idem* 83.

²⁵⁶ *Idem* 134. See the discussion of European recommendations in par 2.3.

²⁵⁷ *WB Report* 83–84 and 134–135. See also Boraine and Roestoff 2014 *THRHR* 539.

²⁵⁸ *WB Report* 84–85. Boraine and Roestoff 2014 *THRHR* 539.

results as decision-makers generally impose excessive terms, which call for proper education regarding the impact that this may have on debtors. It has also led to natural and systemic standardisation, especially where a guideline was available. If the second technique is chosen, the question relates to the optimal duration of the term. There is little uniformity, but it is noted that terms generally range from three to five years. The report suggests that a period of more than three years is irresponsible from a social point of view.²⁵⁹

As payment plans are linked to future income, a pertinent issue relates to the amount of future income that the debtor has at his disposal. How much can be expected from debtors is therefore a core issue and in this regard most agree that the problem is not so much a matter of calculating a predetermined benefit for creditors than determining the debtor's level of sacrifice. The determination of potential payment to creditors commences with a determination of the amount to be reserved for reasonable maintenance of the debtor and his dependants. Only income in excess thereof represents a surplus to be assigned to creditors. Therefore, both income and reasonable support expenses must be evaluated.²⁶⁰ Two approaches can generally be identified in the determination of future income. The first makes use of actual income where creditors are assured of optimal payment. The other is a projection of future income and defines a specific payment for each creditor over the term. Although the latter is the most common, the report refers to the fact that it will be inaccurate in most instances and that both an under- and an over-estimation are problematic. On the other hand, the actual income approach usually involves significant monitoring and administrative burdens. Where a uniform allowance is allocated, calculations may be easier and may be done by employers. Where projected income is used, past income over a specific period, for instance the last six months, should not be used as an estimate of future income as it is likely to result in gross inaccuracy.²⁶¹

²⁵⁹ *Idem* 85–86 and 135. This is in line with the proposals of the Reifner *Report* 253–254; see par 2.3.

²⁶⁰ See WB *Report* 87–88.

²⁶¹ *Idem* 87–89 and 135.

Another important consideration is whether transfer payments, such as social assistance or social support, should be excluded from income. Where insolvency expense allowances are co-ordinated with social assistance standards, this may not be a problem at all. However, it is cumbersome when low-income debtors are wholly reliant on transfer payments and these are diverted to creditors.²⁶²

Once the debtor's income has been determined, another central issue relates to the resources that should be reserved for debtors' support, as a proper balance between benefit for creditors and adequate support for debtors should be attained. Equal treatment of debtors should also be kept in mind. In defining a proper reserve budget to ensure fair and equal treatment, the report considers two basic approaches. The one is a flexible approach based on discretion and the second is a standardised approach. It is said that a flexible approach may be theoretically attractive, but proved to be problematic in practice in especially four ways. The first problem is that decision makers may be too liberal and overly debtor-friendly, contrary to what legislators and policy commentators regard as appropriate. However, a more common and more detrimental problem is exactly the opposite one, where decision makers are too conservative.²⁶³ Thirdly, extreme variations in the exercise of discretion raise concerns of fairness and equal treatment; and lastly, some systems reported a move by decision makers themselves to a more standardised approach.²⁶⁴ It seems that a standardised approach is favoured as the appropriate level of sacrifice in exchange for relief is an inherently political decision that should best be left to the legislature. Judicial and executive actors may have closer contact with and insight into debtors' needs, but are not suited to make such decisions. Discretion does not need to be entirely eliminated but baselines must be established by politically responsible entities.²⁶⁵ Therefore, an optimal approach would allow for some discretionary element in that a standard is supplemented by non-standard allowances such as costs relating to housing, transportation and childcare. The report suggests that such an approach would establish a common and perhaps

²⁶² *Idem* 90. In South Africa, almost the majority of the population is in some way or another reliant on social grants; see ch 1 par 1.1.

²⁶³ The report notes that as many as three-quarters of the plans will fail where modern realities of basic needs are ignored; *WB Report* 92.

²⁶⁴ *WB Report* 91–93.

²⁶⁵ *Idem* 94 and 136.

functional compromise between the undesirable effects of discretion on the one hand and an inflexible strict-standard norm on the other.²⁶⁶

The report suggests that the simplest and most used approach when selecting a basic budgetary standard is to simply view the insolvency system as an extension of the ordinary collection system, where the same limitations on the garnishment of wages and other income are adopted.²⁶⁷ However, these should regularly be revised and adapted in accordance with inflation. The adoption of a uniform standard provides for ‘bands of uniformity’, where debtors are categorised into groups with different exemption amounts. These standards may often be increased for specific variable expenses. Exempt income levels may be dependent on whether the debtor is married, the number of his dependent children and their ages. These figures are then supplemented with reasonable expenses for housing and child care. Where ordinary enforcement restrictions or social assistance minimum incomes are not available or appropriate in insolvency cases, it is suggested that these standards can be built from scratch. It is further suggested that data already available within a specific jurisdiction (such as ‘baskets of standard household items consumed by various family sizes’ during a specific term) can be used to construct basic budgetary standards.²⁶⁸

Deducting standard living expenses from income will in many instances result in little or no surplus being available for distribution. This may occur irrespective of whether administration costs are deducted before distributions are made to creditors. In this respect, some insolvency systems have excluded NINA debtors from relief by discharge as there is no benefit for creditors in NINA cases.²⁶⁹ However, the report suggests that the approach favoured by both commentators and established systems is to avoid discrimination on financial grounds and to provide a discharge to all insolvent debtors. It is mentioned that ‘zero plans’ in any event represent the majority of natural person insolvency cases ranging from 33% to 80% of all matters. In many instances not even the administration costs are covered. A particular

²⁶⁶ *Ibid.*

²⁶⁷ In South Africa, no limitations as regard the percentage of income that may be attached in individual enforcement proceedings is prescribed; ch 1 par 1.1.

²⁶⁸ *WB Report* 94–96 and 136.

²⁶⁹ South Africa is such a system; see ch 1 par 1.1.

jurisdiction's Constitutional Court ruled that extending relief to only those who can pay a portion of their debt violates the equality principle of that country's constitution.²⁷⁰ The report proposes that it is more accurate to refer to 'debt adjustment plans' or 'rehabilitation plans' in these instances. Lawyers waive fees in some systems, others postpone the obligation to pay administration costs, while another's specifically developed formal solution is a low-cost alternative measure that is built into a multi-option system.²⁷¹

Once a plan is confirmed, insolvency representatives are commonly tasked with facilitating its implementation and compliance.²⁷² More particularly, these representatives generally monitor, periodically collect and distribute payments²⁷³ to creditors. Such administration is the representative's most time consuming and resource intensive task and remuneration is generally deducted from surplus income before the remainder is distributed to creditors. The charging of fees against amounts otherwise intended for creditors creates an incentive for creditors to agree to informal arrangements and is further competent as the representative takes care of the monitoring function on behalf of the creditors. The representative is often tasked with objecting to the discharge where the debtor did not meet the necessary requirements. Not all jurisdictions make use of insolvency representatives and in such instances creditors usually bear the burden of monitoring and enforcing such plans.²⁷⁴

The last consideration when devising a payment plan is the need for modification in instances where the debtor's financial position unexpectedly deteriorates or

²⁷⁰ It seems that the report refers to Belgium. See Order No. 3/2003 (3 April 2003) <http://bit.ly/1Lug83Y> (accessed 16 December 2014). See also Kilborn 2006 *Am Bankr Inst L Rev* 94, Kilborn 'Inaugural lecture' 33 and Spooner 2013 *ERPL* 755. For the general position relating to the right to equality in South Africa see ch 1 par 1.1.

²⁷¹ *WB Report* 97–98 and 136. The last-mentioned approach could be a referral to the no-asset procedure in New Zealand; see ch 6 par 6.5.3.

²⁷² As regards insolvency representatives' qualifications see the discussion of the *ICR Standard* in par 2.6.1.

²⁷³ Many systems require annual distributions as more regular distributions increase costs and reduce payments to creditors.

²⁷⁴ *WB Report* 99–100 and 136–137.

improves.²⁷⁵ Where lawyers and court involvement are necessary, a debtor may be unable to request a modification due to financial restraints and therefore some systems rely on the representative to request modifications on behalf of the debtor. It is cautioned that not providing for this need may result in unduly burdensome and costly repeat filings.²⁷⁶

The report measures the ‘advantages and disadvantages of the different approaches to payment’. It observes that although most systems require individuals to be processed through both an asset liquidation and a repayment plan procedure, in order to improve the chances of some return for creditors, this may have significant disadvantages. The basic disadvantage in relation to value extraction is the waste of time, money and other resources as was discussed above. These disadvantages are also in contrast with the primary benefit of a collective approach in natural person insolvency, namely, the prevention of waste and an infertile quest for value. The report suggests that a single official investigation can reveal the foolishness of chasing after low-value assets and preventing creditors from destroying the purely personal value of household items. The same can be said for repayment plans as very few result in any return for creditors. It is further doubtful whether the administrative costs associated with the ‘good behaviour system’ are justified and therefore many commentators and legislators are said to question the value (on mere grounds of retribution) of imposing plans on destitute individuals who do not have the ability to pay. Although there are doubts as to whether repayment plans are effective in achieving the goals of natural person insolvency, they have remained popular in many systems as most legislatures are of the opinion that they serve significant moral and educational purposes.²⁷⁷

Referring to an existing system,²⁷⁸ the report argues that major problems arise where a debtor is allowed to self-select either the liquidation or payment plan procedure. Even the introduction of a means test only resulted in substantial administrative

²⁷⁵ Where actual income and expenses are used to devise a payment plan it will be self-modifying. However, the more common approach makes use of projected income and expenses which call for modification once a change in circumstances occurs.

²⁷⁶ *WB Report* 101–102 and 137.

²⁷⁷ *Idem* 102–105 and 137.

²⁷⁸ Presumably the USA; see par 2.2.

burdens and litigation, whilst not truly increasing payment to creditors. The report favours the approach where the debtor's ability is based on a screening mechanism that focuses on the reality of the situation rather than on presumptions. It further suggests that the sorting function should best be left to disinterested actors.²⁷⁹

The report pays special attention to the payment of mortgages and other secured loans before turning to the last core attribute of an insolvency regime for natural persons, namely, the discharge. It is noted that secured debt does not play a major role in insolvency proceedings as debtors usually do not have valuable assets that can be used as collateral for loans or because such assets have already been foreclosed on. In fact, many jurisdictions subscribe to the notion that debtors should not have secured debt or non-essential assets when filing for insolvency procedures. Others subscribe to a more balanced approach where provision is made for secured assets that are important to the debtor's post-insolvency existence. Nevertheless, secured creditors are in principle protected. This is because the protection of credit markets combined with the constitutional right to property in this regard underscore the strong position of creditors. Policymakers generally fear that an infringement of secured creditors' rights may have a profound impact on the availability of credit to finance important social activities. Such a violation may also destabilise broad sectors of the lending industry and even national economies. However, jurisdictions that subscribe to a more balanced approach acknowledge that a properly structured insolvency system does not cause losses or financial damage as these have already occurred through debtors' inability to pay, which is sometimes aggravated by constantly depressed collateral values. Policymakers in these jurisdictions use legislative measures to force creditors to accept the reality of debtors' positions and/or the loss of value of collaterals. It is noted that such an approach establishes real values, limits losses and forces parties to engage in more sustainable economic relationships.²⁸⁰

As was noted, mortgages receive special attention as they are more important to a debtor than other secured debts. Mortgages can further be distinguished from other

²⁷⁹ *WB Report* 105. Contra the *INSOL* reports that favour the position where the choice of procedure is left to debtors; par 2.5.

²⁸⁰ *WB Report* 105–107 and 137–138.

secured debts both as regards value and the nature of the security that they offer. However, the starting point in most systems is that debtors do not own their homes or cannot retain their homes in personal insolvency proceedings. In these jurisdictions, homes are sold before or during insolvency proceedings and the debtors usually resort under unsecured credit. Conversely, some jurisdictions value homeownership to such an extent that it is, even in insolvency proceedings, protected to some degree.²⁸¹ Furthermore, as large quantities of economic value may be lost in times of financial crisis (where massive numbers of foreclosures take place simultaneously), some countries have either adopted temporary crisis measures or have some form of homeownership protection built into their insolvency system.²⁸² However, no existing system allows for a debtor to retain his home when faced with long-term inability to service his mortgage loan.²⁸³

Some insolvency systems allow debtors to retain certain household items even where they serve as security for debt, as their utility value to the debtor likely outweighs their economic value to the creditor. Automobiles are a good example in this regard. Where such assets are necessary for the household or to earn a living, payments in respect thereof may be included in necessary living costs, which may be subject to the discretion of the courts.²⁸⁴

2.6.2.6 Discharge

The 'discharge' is the last theme investigated as being a core legal attribute of an insolvency system for natural persons. The discussion is structured around its purpose, characteristics and scope, the position of guarantees, co-debtors and third party collateral. As regards purpose and characteristics it is acknowledged that one of the principal objectives of an insolvency system for natural persons is economic rehabilitation. According to the report, this concept has three elements, namely, the discharge of excessive debt, non-discrimination after relief was granted and that the debtor should be competent to avoid excessive debt in future.²⁸⁵ The most effective form of relief is said to be the fresh start – a straight discharge without the necessity

²⁸¹ *Idem* 107–110 and 138. See also the discussion on family home exemptions above; *idem* 79.

²⁸² See *idem* 108–114 and 138 as regards crisis measures.

²⁸³ *Idem* 114.

²⁸⁴ *Idem* 114–115. See also the discussion of exemptions other than the home above; *idem* 80–82.

²⁸⁵ *Idem* 115.

of a repayment plan.²⁸⁶ However, most countries reject the straight-discharge notion and only provide a discharge once certain conditions have been met. These conditions may include a payment plan that runs for a specific period. In this regard, it is better to refer to ‘earned new start’ than to ‘fresh start’.²⁸⁷ As far as the ‘earned new start’ is concerned, it is mentioned that where systems require minimum payment before the discharge is awarded, many honest but unfortunate debtors will not qualify and therefore some countries have decided that such requirement will result in discrimination against those with little or no means. The report advises that when considering the introduction of a payment plan procedure, a realistic assessment of the factual situation will lead to more tolerant and shorter plans as opposed to focusing attention on general private law principles such as *pacta sunt servanda*.²⁸⁸

The second element of rehabilitation supports the first, namely, non-discrimination during and after completion of the repayment plan. This is so since actual rehabilitation is achieved by treating debtors as the equals of non-debtors once relief is granted. In this regard, some countries’ data protection regulations prohibit the registration and use of insolvency information once a plan has been completed, while others retain negative credit entries for a number of years. The report cautions that non-discrimination is a serious issue that needs to be considered when striving to achieve the full benefit of a discharge.²⁸⁹

The third element of rehabilitation is the healthier and more responsible use of credit. However, this is difficult to achieve or measure. An attempt to address this element is the prohibition of repeat filings that is generally present in all systems. There has also been increased interest in financial education and debt counselling, as many debtors do not have adequate financial skills. However, resources are limited and doubts exist as to the efficiency thereof.²⁹⁰ Another manner in which jurisdictions

²⁸⁶ See the discussion of the fresh start and in particular the historical straight discharge that was available in the USA before the enactment of BAPCPA; par 2.2.

²⁸⁷ See the discussion of European recommendations; par 2.3.

²⁸⁸ WB Report 115–116 and 138 and Boraïne and Roestoff 2014 *THRHR* 540; see also par 2.2 and ch 1 par 1.1.

²⁸⁹ WB Report 116–117 and 138–139. See also Boraïne and Roestoff 2014 *THRHR* 541.

²⁹⁰ Contrary to the INSOL reports that advocate debt counselling; par 2.5.

strive to inculcate healthier and more responsible use of credit is to force debtors to execute a repayment plan as was discussed above. A related issue is the good faith requirement that is found in almost all jurisdictions. In this regard, the system may require debtors, as a prerequisite for a discharge, to disclose their economic affairs. Countries also attempt to address moral hazard (which is difficult to assess) by denying the discharge of debt that was recklessly, unscrupulously or speculatively incurred. Indeed, all jurisdictions prohibit an abuse of the insolvency system and will deny a discharge where it occurs, although the manner in which it is enforced may differ.²⁹¹

As regards the scope of the discharge, it is noted that in order to achieve effective rehabilitation and its related goals, as many debts as possible should be included in the discharge. Furthermore, the equal treatment of creditors does not generally allow for many exceptions thereto. This being said, all jurisdictions make provision for some exceptions and these mostly relate to non-market based debts. Maintenance debts and public obligations are mentioned in particular. The basic policy reasons for the exclusion of maintenance debts, beyond their non-market based nature, are the proper allocation of responsibility and burden as well as the general unwillingness to allow debtors to shift their most fundamental responsibilities onto other vulnerable parties. It is submitted that the protection of maintenance claims is just as important as the discharge to the debtor. Fines and other sanctions as a consequence of crime are also generally excluded on the basis of the proper allocation of responsibility.²⁹² The report thirdly considers taxes and other non-punitive government debts, which have historically been excluded on the same grounds as family responsibility debts, although a trend to abolish the special treatment of these debts has developed for mainly two reasons. Firstly, such debts are often the largest and their exclusion will therefore undermine the whole system. Secondly, if these non-punitive debts are not excluded, they usually rank higher in priority, which has been criticised as being unfair towards other creditors. The report mentions that although educational loans

²⁹¹ WB Report 117–118 and 139. Boraine and Roestoff 2014 *THRHR* 541.

²⁹² Some systems extend this reasoning to personal and property damage claims where some form of culpable conduct can be detected.

are excluded in a few jurisdictions, it is a controversial topic.²⁹³ Reaffirmation agreements between debtors and creditors during insolvency proceedings are also considered in the report. These are used to exempt certain debts from a discharge. It is mentioned that such agreements have been forbidden in some countries as they constitute a violation of the principle of creditor equality. However, others allow them subject to court approval and on condition that they serve the debtor and are voluntarily affirmed by him. The report finally comments on post-commencement debts and notes that even though a debtor should be cautious not to incur new debt during the duration of the payment plan, it is a very valuable instrument in debt restructuring.²⁹⁴

Family members often personally guarantee debts or put up their assets as collateral security in favour of other family members. This is the last topic discussed under the discharge issue. Few jurisdictions regulate these matters and therefore insolvency proceedings and the discharge generally have no easing effect on guarantors, which is in line with the very aim of securities, namely, to ensure that the debt is serviced in the event that the debtor becomes insolvent. However, there is an argument that those who are dependent on the debtor or who have strong emotional ties with him should be protected against abusive contracts. Strong arguments are made in favour of the information rights of guarantors and restrictions on family members as guarantors.²⁹⁵

2.6.3 Synopsis

From the discussion of the World Bank *Report* its hesitance to specifically prescribe a set of 'best practices' as regards natural person insolvency systems is clear, although some preferences can certainly be detected. However, most of the dialogues are so involved in either motivating the need for proper functioning insolvency systems or discoursing all possible attributes of insolvency regimes for

²⁹³ The reasons behind such exclusions are that they represent an investment in the debtor's future and should be paid from future benefits flowing from this very investment. Such debts may further be quite significant and where a central state lending authority is responsible for extending these loans it may place an undue burden on it. However, it is noted that some debtors do not have any prospect of significant income in future and many systems do not regard the exclusion of these debts as the optimal solution.

²⁹⁴ *WB Report* 118–122 and 139.

²⁹⁵ *Idem* 122–125 and 139–140.

natural persons that they represent a labyrinth of themes, making it particularly difficult to cohesively summarise the outcomes of the study. Nevertheless, some of the detail is of importance and will be used in subsequent chapters to evaluate the more intricate parts of the South African system.

Even though the extraction of a clear set of endorsements is difficult, Kilborn has identified three most salient themes which he describes as ‘high-level guidelines by which to evaluate existing and new personal insolvency systems’.²⁹⁶ The first is the need to implement formal legal measures by which debt relief is granted to over-indebted persons through a forced discharge of some or all debt. This is consistent with previous recommendations made by international organisations.²⁹⁷ Secondly, he suggests that the report takes note of the widespread preference for informal negotiated workouts (as opposed to making use of the formal system), but that it separates itself from former reports in that the practical difficulties inherent to this ‘theoretically attractive goal’ are emphasised. He states that the benefits of informal negotiations are often illusory and that such attempts most often fail.²⁹⁸ The third most prominent theme is that generally some conditions for relief are set. In other words, something is expected in return for a discharge of debt, which ties in with the emphasis that is placed on the need for a balance as regards debtors’ and creditors’ interests. In this respect, almost all jurisdictions expect debtors to proceed through a repayment plan and to make some level of payment towards their creditors in earning their fresh start. Inherent in this theme is the call for cautious plan formulation to not unduly burden debtors, a recommendation which is also detected in other reports.²⁹⁹

2.7 Conclusion

The aim of this chapter is to extract the internationally regarded elements of an effective and efficient natural person insolvency system, which can be regarded as being equally relevant in all jurisdictions, in order to provide a framework of the most commonly shared recommendations set by the international community, against

²⁹⁶ Kilborn 2014 *PILR* 4.

²⁹⁷ *Idem* 4–5.

²⁹⁸ *Idem* 5.

²⁹⁹ *Idem* 5–6.

which jurisdictions considered in this thesis are measured. The fresh-start trend, which had its origins in the USA, and which is widely regarded as having liberalised the field of natural person insolvency law, as well as some developments within the European context and France, were referred to. The American system and the broader European developments provided a background to a discussion of the universal principles and guidelines as they strongly influenced international recommendations. The French administrative approach was referred to as its novel initiative in involving its central bank in natural person insolvency matters has proved to be a very effective endeavour. This innovation has led to a reduction in the system's administrative burden without compromising the relief offered. Such outcomes are important from developing countries' points of view. What can, amongst others, be learned from them is that those responsible for reform should not be hesitant to search for answers in unlikely corners. However, principles and guidelines stemming from the most prominent international reports, namely, the *INSOL International Consumer debt reports* and the *World Bank Report on the treatment of the insolvency of natural persons* took centre stage. This paragraph provides a summary of the essential elements of a functioning natural person insolvency system that responds to contemporary needs. The ultimate aim of devising this framework is to eventually draw from it in considering possible solutions to potential shortcomings specifically in the South African natural person insolvency system. The warning against the adoption of a mainstream approach is observed and, therefore, discussions in subsequent chapters take cognisance of the adjacent environment of laws, policies and practices. Nevertheless, the observation by Spooner that inherently national factors should not be over-emphasised is kept in mind.³⁰⁰

However, before proceeding with a summary of the essential elements of a functioning natural person insolvency system, three rudimentary assumptions, flowing from discussions in this chapter, are acknowledged and accepted. The first is that an effective natural person insolvency system is a necessity in modern credit-driven economies; secondly and closely related to the first assumption is that, although the introduction of or developments in natural person insolvency systems

³⁰⁰ Spooner 2013 *ERPL* 774 *et seq.*

may pose concerns along the lines of debtors' moral hazard, fraud and stigma, the many benefits of a progressive system outweigh such concerns, which can be overcome; and thirdly, a balance between the rights of debtors, creditors and society (the three beneficiaries of effective distressed debt regulation) should be maintained.³⁰¹

From the discussion in this chapter, the following aspects are identified as essential elements (which overlap in many instances) of an effective natural person insolvency system:

a. Access to all honest but unfortunate debtors

Access seems to be a non-negotiable element and therefore all *bona fide* debtors should in principle be assisted. Access should be restricted only in cases of fraud or serious misconduct.³⁰² Related to this principle is the idea that costs should not pose an obstacle to access.³⁰³ Another associated issue that flows naturally from the basic premises of access for all is that discrimination on financial grounds ought to be avoided and that NINA debtors should therefore be able to enter the system.³⁰⁴

Some ancillary issues are that the liquidity test for insolvency is preferred as an access requirement, and that assessment should be based on the debtor's current inability to meet present debts. Furthermore, in instances where creditors are allowed to file insolvency procedures, guarding against potential misuse calls for regulation. An issue associated with the possibility of creditors' petitions is that acts of bankruptcy are out-dated as the focus should be on the inability to pay, as opposed to wrongful actions of the debtor.³⁰⁵

b. Discharge

The discharge of pre-insolvency debt features most prominently in this chapter. This is because one of the principal objectives of an insolvency system for natural persons is economic rehabilitation. A discharge should therefore be possible and as

³⁰¹ European reports par 2.3; INSOL reports par 2.5.

³⁰² This is universally accepted by all reports.

³⁰³ Huls *Report* par 2.3; INSOL reports par 2.5.2.

³⁰⁴ WB *Report* par 2.6.2.5.

³⁰⁵ *Idem* par 2.6.2.3.

wide as possible as several exclusions may hinder a fresh start.³⁰⁶ Drafters are cautioned against creating a perception that insolvency procedures provide an easy way out as this will impact on society's willingness to allow a fresh start. However, debtors should not be disheartened or alienated from society by unnecessary restrictions.³⁰⁷ The discharge may be partial in that the debtor may be required to pay a portion of the debt in accordance with his means, although a total discharge should be allowed in hardship cases.³⁰⁸ The discharge should not be too distant in the future³⁰⁹ and should not be based on a certain level of payment to creditors, which is in line with the prohibition against discrimination on financial grounds.³¹⁰ Good behaviour may be set as a condition for the discharge and creditors and state agencies can play a role in challenging same – yet the criteria for challenges should be clear.³¹¹

As the discharge must be as wide as possible, exceptions thereto should be limited. Secured debt is generally excluded from the discharge. In instances where secured assets are important for the debtor's post-insolvency existence, provision should be made therefor in living expenses, which may be subject to court approval.³¹² Furthermore, the exception of alimonies especially for children is accepted, although exceptions for taxes, fines and damages are not recommended.³¹³

Closely related to the discharge of pre-insolvency debt are exemption laws as they improve the outcome of the discharge, in that debtors are provided with the necessities to continue with their lives. Therefore, some consideration as regards the protection of assets and income is necessary as the right to a decent living standard should be respected.³¹⁴ In this regard, a general standards-based approach is favoured where most property is exempted and where the obligation to claim assets of excess value is placed on the insolvency representative. The reasoning behind

³⁰⁶ See the position in the USA par 2.2; European reports par 2.3; INSOL reports par 2.5.2 and 2.5.3; and *WB Report* par 2.6.2.6.

³⁰⁷ INSOL reports par 2.5.3.

³⁰⁸ *Huls Report* par 2.3.

³⁰⁹ *Ibid* and *EC Best project report* par 2.3.

³¹⁰ USA par 2.2; European reports par 2.3; INSOL reports par 2.5.4 and *WB Report* par 2.6.2.6.

³¹¹ *WB Report* par 2.6.2.3.

³¹² *Idem* 2.6.2.5.

³¹³ See European reports par 2.3 and *WB Report* 2.6.2.6.

³¹⁴ See *Reifner Report* par 2.3 and *WB Report* par 2.6.2.5.

these suggestions is that assets are generally more valuable to the debtor than what their economic value represents. This approach may be most efficient in jurisdictions where the majority of insolvents have limited personal assets.³¹⁵ In line with the increased focus on debtor rehabilitation, higher limits of exemptions should be established.³¹⁶

The purest form of and most liberal route to a discharge was the American pre-BAPCPA measure, generally referred to as the ‘straight discharge’. This can be contrasted with the European stance that rather opts for an ‘earned new start’. However, the American system has journeyed to a more balanced approach, which is now more closely aligned with European attitudes. It is no longer openly accessed (in the sense that a debtor has a choice as to his preferred debt relief measure) as BAPCPA has introduced a means test that channels debtors to the most appropriate route in instances where income exceeds a median in the debtor’s state of residence. Nevertheless, much-deserved criticism has been levelled against BAPCPA’s ‘anti-fraud’ measures. However, it seems that the ‘earned new start’ is globally more acceptable although the manner in which this preference should be executed must be meticulously designed in order to prevent the waste in which BAPCPA’s provisions have resulted.

c. Multiple procedures depending on the debtor’s circumstances

It is commonly accepted that alternative debt relief measures (to bankruptcy) are needed and that the alternative of choice should depend on debtors’ differing circumstances and merits.³¹⁷ Generally, asset liquidation procedures, repayment plan procedures and procedures suited to NINA debtors’ needs are mentioned. Unfortunately, not one of the reports provides exact guidelines as to how a NINA procedure should be devised. However, it is cautioned that in developing all natural person insolvency procedures, the important reality, namely, that an attempt to extract value from natural person insolvents will result in many complications, should

³¹⁵ WB Report par 2.6.2.5.

³¹⁶ *Ibid.*

³¹⁷ Cork Report par 2.3; INSOL reports par 2.5.2.

be kept in mind.³¹⁸ Furthermore, it is not appropriate to require that individuals be subjected to both an asset liquidation and a repayment plan procedure.³¹⁹

Some common remarks equally relevant to all procedures are that once a case has been filed, a moratorium on debt enforcement should kick in.³²⁰ Creditor participation should as a matter of course be excluded, except in instances where the estate represents significant value.³²¹

When considering the formulation of a liquidation procedure, it is imperative to recognise that the focus on assets is usually all but a formality as most debtors do not have assets of value. In any event, the liquidation procedure links with property exemptions and in this regard a standards-based approach that, as a matter of course, exempts most property from the estate would be best suited to jurisdictions where debtors have limited personal assets. This is because levels of sufficiency are, in line with the focus on rehabilitation, central to modern systems.³²²

As regards the repayment plan (rehabilitation procedure), it seems that it mostly serves moral and educational purposes as, in modern systems, the focus should be on rehabilitation and a level of self-efficiency.³²³ The twin issues of duration and payment feature most dominantly in system design.³²⁴ It is widely proposed that plans should be realistic and a period of between three and five years is generally preferred,³²⁵ although the *WB Report* states that a period of more than three years is irresponsible from a social point of view.³²⁶ During this period, non-exempt assets and net earnings should be used to service debt, as the debtor should do the best that he can to be rewarded with the discharge at the end of the term.³²⁷ What can be expected of debtors should be based on the desired level of debtors' sacrifice, rather than the level of benefit to creditors. In this regard, the amount to be reserved for

³¹⁸ *WB Report* par 2.6.2.5.

³¹⁹ *Ibid.*

³²⁰ *Cork Report* and *Huls Report* par 2.3; and *INSOL reports* par 2.5.2.

³²¹ *WB Report* par 2.6.2.4.

³²² *Idem* par 2.6.2.5.

³²³ *Ibid.*

³²⁴ See *WB Report* par 2.6.2.5.

³²⁵ See European reports par 2.3 and *WB Report* par 2.6.2.5.

³²⁶ *WB Report* par 2.6.2.5.

³²⁷ *Huls Report* par 2.3.

reasonable maintenance of the debtor and his dependants constitutes the starting point and a standardised approach is favoured. This is because the appropriate level of sacrifice, in exchange for relief, is inherently political – although limited discretion is important. A standard should consequently be supplemented by non-standard allowances such as costs relating to housing, transport and childcare.³²⁸

A last observation as regards ‘multiple procedures’ is that international guidelines are not in agreement as to whether the choice of accessing a particular procedure should be left with the debtor or a disinterested third party. However, the most contemporary report, that of the World Bank, clearly prefers that the decision should be left in the hands of public agencies.³²⁹

d. Administration: Judicial versus extra-judicial and informal versus formal procedures

It appears that courts will always have a role to play in natural person insolvency law,³³⁰ but that their involvement should be the exception rather than the rule.³³¹ Even though court participation should be minimised, the execution of a court’s functions should be specialised, as many reports refers to ‘insolvency courts’.³³² The remaining functions of the courts should be counterbalanced by public administrative bodies, which should be strengthened.³³³ However, developing countries should consider the context of existing institutions as such jurisdictions may have to incur significant costs in establishing new nationwide infrastructures. It is suggested that existing institutional infrastructures should rather be extended and that procedures be simplified.³³⁴

The unique French system offers an interesting example of reducing court involvement and general administration. Much bureaucratic and unnecessary red tape was removed in that the French central bank is nowadays almost entirely

³²⁸ WB Report par 2.6.2.5.

³²⁹ WB Report par 2.6.2.3. The INSOL reports in turn favour the position where the debtor is free to choose between procedures; par 2.5.2.

³³⁰ Reifner Report par 2.3 and WB Report par 2.6.2.1.

³³¹ *Idem* par 2.6.2.2.

³³² See Cork Report and EU Best project report par 2.3.

³³³ See Cork Report par 2.3.

³³⁴ WB Report par 2.6.2.2.

responsible for the administration of the insolvency system. This initiative has also led to a buy-in from creditors who are usually resistant to (new) insolvency procedures.³³⁵ It is thus suggested that at least the involvement of a jurisdiction's central bank should be considered in developing a country's insolvency law objectives and devising such procedures, not least as such participation can significantly enhance the credibility of any insolvency system.³³⁶

As regards formal versus informal procedures, it appears that although informal procedures are generally favoured,³³⁷ certain elements are needed to enhance its efficiency. However, the *WB Report* does not support the encouragement of informal procedures as it argues that their benefits are mostly illusory.³³⁸ Nevertheless, and as is the case with other reports, the *WB Report* suggests that certain elements may potentially enhance the probability of informal procedures' success. Such initiatives include the possibility of formal procedures where informal initiatives fail, adequate legal aid or debt counselling and a cram down where a majority vote is obtained. Passive creditors should also not be allowed to hinder agreements³³⁹ and costs should not pose an obstacle to resolving financial problems via an informal route.³⁴⁰ Furthermore, negotiations should proceed without an immediate threat of enforcement.³⁴¹ Some reports favour the position where the roles of the debt counsellor and trustee should be kept separate, whilst others do not see a problem where they overlap, provided that these intermediaries are equipped, independent and professional.³⁴² A call for impartiality as well as proper training, financing and supervision of intermediaries features prominently. Standardised norms, practices and codes of conduct should further be developed.³⁴³

³³⁵ See par 2.4.

³³⁶ See the South African Reserve Bank's intervention in African Bank's financial difficulties in ch 1 par 1.1. However, it does not involve itself in natural person insolvency matters at present.

³³⁷ *Huls Report* and *Reifner Report* par 2.3; *INSOL reports* par 2.5.4.

³³⁸ See *WB Report* par 2.6.2.1.

³³⁹ See European reports par 2.3 and *WB Report* par 2.5.6.1.

³⁴⁰ *INSOL reports* par 2.5.4.

³⁴¹ *WB Report* par 2.5.6.1.

³⁴² See *Huls Report* versus *Reifner Report* par 2.3.

³⁴³ See European reports par 2.3 and *INSOL reports* par 2.5.4 and 2.5.5.

e. *Financing issues*

It is generally accepted that costs should not constitute a barrier to accessing debt relief and that all parties that benefit (socially and economically) from the procedure should contribute to its costs.³⁴⁴ It is suggested that creditors may contribute through a levy.³⁴⁵ The manner in which this suggestion should be executed is not clear and it is proposed that the market segment that a particular credit provider represents may serve as a starting point in calculating his liability. Of course only his involvement in unsecured credit must be taken into consideration as secured credit is generally not affected by an insolvency system. A creditor's involvement in reckless credit extension could also be an indicator of his level of responsibility.

f. *Non discrimination*

Non-discrimination on financial grounds as regards both entrance and discharge should be eliminated.³⁴⁶ The stigmatising effects of bankruptcy should also be reduced, for instance by removing obsolete and damaging restrictions, disqualifications and prohibitions. This will encourage effective financial and social inclusion of debtors and their families. Once a discharge has been granted, the debtor should have full access to financial activities.³⁴⁷

Finally, a remark by Boraine and Roestoff, after considering the principles set out in the World Bank *Report* in relation to the South African natural person insolvency landscape, sets the scene for some of the discussions in subsequent chapters. With the World Bank guidelines as background, they submit that³⁴⁸

[t]he quest should thus be to reform our insolvency law as far as it relates to consumers in such a way as to align it with modern consumer credit realities rather than tinkering with various statutory procedures without addressing cardinal issues that exist.

³⁴⁴ European reports par 2.3 and WB *Report* par 2.6.2.2.

³⁴⁵ WB *Report* par 2.6.2.2.

³⁴⁶ *Idem* 2.6.2.5.

³⁴⁷ Reifner *Report* and EC *Best project report* par 2.3; INSOL reports par 2.4.5; WB *Report* 2.6.2.6.

³⁴⁸ Boraine and Roestoff 2014 *THRHR* 546.

CHAPTER 3: NATURAL PERSON DEBT RELIEF IN TERMS OF THE INSOLVENCY ACT 24 OF 1936

SUMMARY

- 3.1 Introduction
 - 3.2 Brief historical overview
 - 3.3 Aspects of sequestration and rehabilitation
 - 3.4 Statutory composition
 - 3.5 Evaluation in terms of the right to equality
 - 3.6 Conclusion
-

3.1 Introduction

The Insolvency Act of 1936¹ provides for the main debt relief measure in South African insolvency law, namely, the sequestration order procedure. Despite its archaic state, it is (still) considered to be the primary debt relief measure for natural persons in South Africa as it is the only procedure that provides a discharge of debt,² although the discharge is not the main aim thereof.³ Nevertheless, not all over-indebted or insolvent natural persons will qualify for the procedure, mainly because of the advantage for creditors requirement that encompasses the essence of the procedure⁴ – contrary to international trends and best practice.⁵ Due to the exclusivity of the procedure and the reasons therefor, a financially over-committed natural person debtor in South Africa can be ‘too broke to go bankrupt’.⁶ Another debt relief measure provided for by the Act is the statutory composition in terms of which a debtor and his creditors can reach an agreement that claims will be paid, in part or in full, in full and final

¹ 24 of 1936 (hereafter ‘the Act’ or ‘the Insolvency Act’).

² S 129. Compare ch 4 of this thesis.

³ See *Ex parte Pillay; Mayet v Pillay* 1955 (2) SA 311 (N); *R v Meer* 1957 (3) SA 619 (N); *Fesi v Absa Bank Ltd* 2000 (1) SA 502 (C); *Ex parte Ford* 2009 (3) SA 383 (WCC) and *Ex parte Shmukler-Tshiko* 2013 JOL 2999 (GSJ) in general. See Borraine and Roestoff 2014 *THRHR* 365 *et seq* and 371 *et seq* for a discussion of the latter case.

⁴ See ss 6(1), 10(c) and 12(1)(c).

⁵ See ch 2 par 2.7.

⁶ Rochelle 1996 *TSAR* 319.

settlement.⁷ As the procedure is only available after a sequestration order has been granted, it will also not assist those who are excluded from the sequestration procedure.

In line with the theme of this thesis, this chapter sets out to investigate aspects of the Insolvency Act relating to debt relief. This is done to determine the extent to which the Act provides debt relief to overcommitted natural person debtors in South Africa and to consider its effectiveness within the South African context. The investigation includes an evaluation of the debt relief that the Act offers in light of the right to equality as entrenched in the South African Constitution⁸ and which is further built upon by the Promotion of Equality and Prevention of Unfair Discrimination Act.⁹ Throughout this chapter, the relief offered as well as the manner in which procedures are devised and executed are measured against international principles and guidelines.¹⁰

As regards the structure of this chapter, paragraph two deals with the origins of South African insolvency law and briefly explains how the system has developed. Execution and debt relief procedures in Roman law are briefly discussed. The incorporation and development of Roman law in Roman-Dutch law are thereafter considered, as it forms the basis of South African insolvency law. Finally, the statutory developments ranging from ordinances in the different colonies to the existing Act are briefly set out.

Aspects of the Insolvency Act relating to debt relief are discussed in paragraphs three and four. Paragraph three provides an overview of the sequestration procedure. Access requirements relating to both the voluntary surrender and compulsory proceedings are set out to illustrate the differences between the two procedures and to illustrate the difficulty that natural person debtors face in applying for relief. Special emphasis is placed on the advantage for creditors requirement which seems to constitute the most important factor in the

⁷ S 119.

⁸ The Constitution of the Republic of South Africa of 1996 (hereafter the 'Constitution'); see ch 1 par 1.1.

⁹ 4 of 2000 (hereafter the 'Equality Act').

¹⁰ See in general ch 2 and more specifically ch 2 par 2.7.

determination of whether a sequestration order should be granted. Because the formal requirements and the burden of proof are stricter in the case of voluntary surrender proceedings, many natural person insolvents opt for the compulsory route where they request a friend or family member to bring an application for their compulsory sequestration. The judiciary's attitude towards both friendly compulsory applications and voluntary surrender applications aimed at obtaining debt relief is also considered and possible law reform is reflected on. Another aspect under consideration is the impact of secondary statutory debt relief procedures (and especially the debt review procedure in terms of the National Credit Act¹¹) on an application for voluntary surrender.¹² Excluded or exempted assets are considered due to their direct link to the actual relief offered and the probability that the debtor will obtain a true fresh start. The important matter of the debtor's rehabilitation is also considered.

Paragraph four deals with the statutory composition contained in section 119 of the Act. Paragraph five continues the evaluation of South African debt relief measures in light of the right to equality by specifically considering the sequestration procedure. Paragraph six concludes this chapter.

3.2 Brief historical overview

South African insolvency law has its origins in Roman law.¹³ Roman insolvency law under the Twelve Tables was initially penal in nature¹⁴ and provided an option for creditors of a defaulting debtor to execute against the debtor's person by either selling him into slavery, the *manus injectio*, or (allegedly) cutting up and selling his body. Slavery was later substituted with imprisonment. Only much later did the praetor establish a mechanism for execution against the debtor's property, which was known as *missio in possessionem*.¹⁵ This measure broadly permitted a creditor or creditors to attach, protect and advertise the debtor's

¹¹ 34 of 2005 (hereafter 'the NCA').

¹² See ch 4 para 4.2.5 and 4.3.3.

¹³ For a detailed discussion of execution and debt relief measures in Roman law see Roestoff *in Kritiese evaluasie* 13–45.

¹⁴ *Contra* modern law where the purpose is settlement of debt. *Idem* 17 and authorities cited there.

¹⁵ See in general *idem* 16–26.

assets. Creditors could also choose a *magister bonorum* from amongst the group of creditors to oversee the sale of assets, whereupon the whole estate was sold *en bloc* and transferred in accordance with the highest bid (this was known as *bonorum emptio*). Some creditors ranked as preferent creditors. The *magister* was later replaced by a curator – subject to the praetor’s sanction — who sold the estate in lots. This modified measure was known as *bonorum distractio*. It follows from the above that early Roman insolvency law was created solely in the interest of creditors with no consideration for the debtor’s plight. Only later did the *lex Julia* provide for a debtor to surrender his estate to prevent an execution against his person. This was known as *cessio bonorum*,¹⁶ which could apparently be claimed as a right, although it did not provide for a discharge of debt. Property subsequently acquired, except for the retention of enough to sustain the debtor (*beneficium competentiae*), was subject to the procedure. However, the debtor did receive a grace period of one year during which creditor execution was prohibited.¹⁷

Cessio bonorum became part of Roman-Dutch law¹⁸ when it was introduced in Holland. However, in Dutch law it was considered a privilege and was subject to the court’s discretion. The procedure was only available to those who became insolvent due to misfortune and after full disclosure and on notice to creditors. Debtors also had to provide a well set-out procedure. The estate was initially administered by commissioners, under supervision of local magistrates, but was later entrusted to chambers known as *Desolate Boedelkamers*. The *missio in possessionem*¹⁹ was also apparently practised to some extent in Holland. Special ordinances applied, the most important for purposes of this discussion being that of Amsterdam²⁰ as it forms the basis of a large part of South African insolvency law.²¹ A debtor could utilise the relief offered by this ordinance through *cessio bonorum* or by stopping payment. It further established a

¹⁶ *Idem* 26–28.

¹⁷ Bertelsmann *et al Mars* 6–7.

¹⁸ For a detailed general discussion of Roman-Dutch law in the context of insolvency law see Roestoff *in Kritiese evaluasie* 47–69. See *idem* 48–51 for a discussion of the reception of *cessio bonorum* in Roman-Dutch law.

¹⁹ For a discussion of the *missio in possessionem* in Roman-Dutch law see *idem* 51–52.

²⁰ For a discussion of the Amsterdam Ordinance of 1777 see *idem* 53–58.

²¹ *Fairlie v Raubenheimer* 1935 AD 146.

chamber that was tasked with the administration of the estate. The Amsterdam Ordinance also introduced the concept of rehabilitation and the subsequent discharge of pre-sequestration debt – where a majority of creditors voted for it. In this regard Roestoff notes that rehabilitation was the most important development that the ordinance brought about.²² Another form of relief offered by Roman-Dutch law, called *surchéance van betaalinge*, was a suspension of payment and the prohibition of execution for a year.²³

It seems that early Cape law made provision for the two types of relief that were observed in Roman-Dutch law. In 1803, the *Desolate Boedelkamer* was founded which, amongst others, administered insolvent estates. However, Bertelsmann *et al* note two significant deviations from the Amsterdam Ordinance, namely, that creditors could not directly secure a debtor's sequestration and that they did not take part in the administration of the estate. The *Desolate Boedelkamer* was later replaced by a system in which a sequestrator took over its functions and later the office of sequestrator made way for the office of the commissioner which was then tasked with the administration of sequestrated estates.²⁴

The Cape Colony passed various ordinances, the most important being Ordinance 6 of 1843.²⁵ This ordinance abolished *cessio bonorum*²⁶ and the right of *surchéance van betaalinge*.²⁷ It made provision for a voluntary surrender of the debtor's estate²⁸ as well as a compulsory sequestration procedure by a creditor or creditors.²⁹ It also provided for rehabilitation, where debts were discharged if accepted by a specified majority,³⁰ and a statutory composition.³¹ However, civil imprisonment was still a possibility.³² This ordinance can be seen as the foundation of South African insolvency law as it was largely adopted in the then

²² Roestoff *n Kritiese evaluasie* 57–58 and 67.

²³ Bertelsmann *et al Mars* 8–9.

²⁴ *Idem* 9–10. See also Roestoff *n Kritiese evaluasie* 311–315.

²⁵ For a discussion of the ordinance see Roestoff *n Kritiese evaluasie* 322–327.

²⁶ S 2 Ordinance 6 of 1843.

²⁷ See *Newcombe v O'Brien* 20 EDC 296.

²⁸ S 2.

²⁹ S 5.

³⁰ S 117 read together with s 120.

³¹ S 106.

³² S 124.

Natal, Orange Free State and Transvaal.³³ After independence, the Union of South Africa replaced the insolvency laws in the various provinces with one Insolvency Act,³⁴ which also strongly resembled the Cape Ordinance. An interesting attribute was that the 1916 Act did not require proof of advantage for creditors in voluntary surrender applications although it did consider such interests.³⁵ It also seems that some courts viewed voluntary surrender as a true debt relief measure.³⁶ Further significant developments were that no provision was made for civil imprisonment of unrehabilitated insolvents, that the specified majority vote of creditors in lieu of a statutory composition was relaxed³⁷ and that the Act did not require a creditors' vote on whether the insolvent was eligible for rehabilitation.³⁸ The 1916 Act also made provision for a separate debt relief measure, namely, statutory 'boedelafstand'.³⁹ As this measure was apparently misused by debtors it was not taken up in the existing Insolvency Act that came into effect on 1 July 1936.⁴⁰

As regards the origins of South African insolvency law, it is important to note that the Insolvency Act does not affect common-law rights that are not in conflict with it. Furthermore, the South African courts sometimes turn to English law where Roman-Dutch law is silent on a particular matter.⁴¹

When considering the early origins of the South African insolvency law, a few notable correlations with contemporary international principles and guidelines can be identified.⁴² So, for example, already in Roman law *cessio bonorum* could

³³ See Bertelsmann *et al Mars* 11 and authorities cited there.

³⁴ 32 of 1916 (hereafter 'the 1916 Act'). This Act was subsequently amended by Act 29 of 1926 and later by Act 58 of 1934. See in general Roestoff *in Kritiese evaluasie* 327–330 for a discussion of the most pertinent aspects of the 1916 Act.

³⁵ S 3.

³⁶ See *Ex parte Terblanche* 1924 TPD 172.

³⁷ S 105.

³⁸ S 108.

³⁹ Ss 115–128.

⁴⁰ The Insolvency Act, which has been amended on various occasions. Some of the amendments were the Insolvency Law Amendment Act 16 of 1943, Insolvency Amendment Act 99 of 1965, Insolvency Amendment Act 101 of 1983, Insolvency Amendment Act 122 of 1993, Insolvency Amendment Act 32 of 1995, Insolvency Amendment Act 33 of 2002 and the Insolvency Second Amendment Act 69 of 2002.

⁴¹ Bertelsmann *et al Mars* 16. See ch 7 for a discussion of the natural person insolvency law in England and Wales.

⁴² See ch 2 par 2.7.

have been claimed as a right and provision was made for a moratorium on the enforcement of debt. Also, the Amsterdam Ordinance provided for rehabilitation and a subsequent discharge of debt, although this was only possible if a majority of creditors consented thereto. In early Cape law, public agencies administered insolvent estates. Furthermore, creditors could not directly secure a debtor's sequestration and did not take part in the administration of the estate. The 1916 Insolvency Act in turn did not contain the advantage for creditors requirement in relation to voluntary surrender applications with some courts regarding the procedure as a true debt relief measure.

3.3 Aspects of sequestration and rehabilitation

3.3.1 Overview of the process

The main object of the Insolvency Act is to regulate the sequestration process by ensuring an orderly and fair distribution of assets for the advantage of the creditors of an insolvent estate.⁴³ However, this objective is contrary to modern international principles and guidelines which focus on the financial rehabilitation of insolvent debtors.⁴⁴ Borraine and Van Heerden state that because of the extensive nature of sequestration it should be viewed as⁴⁵

a sui generis mechanism that sets a collective procedure in motion aimed at administering an insolvent estate on behalf of the insolvent's group of creditors in order to achieve an equitable distribution of the insolvent's assets.

The creditors referred to above are the creditors as an entity or the *concursum creditorum*⁴⁶ which is established once the order for sequestration is granted.

The legal position was explained as follows in *Walker v Syfret NO*:⁴⁷

[T]he hand of the law is laid upon the estate, and at once the rights of the general body of creditors have to be taken into consideration. No transaction can thereafter be entered into with regard to estate matters by a single creditor to the prejudice of the general body. The claim of each creditor must be dealt with as it existed at the issue of the order.

⁴³ See Bertelsmann *et al Mars* 2; Smith 1985 *MB* 27 and Evans and Haskins 1990 *SA Merc LJ* 246.

⁴⁴ Ch 2 par 2.7.

⁴⁵ Borraine and Van Heerden 2010 *PELJ* 111.

⁴⁶ See *Walker v Syfret* 1911 *AD* 166; Bertelsmann *et al Mars* 2; and Smith 1985 *MB* 27.

⁴⁷ 166.

The sequestration order may be applied for by a creditor or creditors⁴⁸ of the debtor in which case the process is referred to as a compulsory sequestration. Nevertheless, international principles and guidelines are sceptic of creditor applications as they can be misused.⁴⁹ The debtor can also apply himself,⁵⁰ in which instance the term ‘voluntary surrender’ is used. In the latter instance the formal requirements and the burden of proof are stricter.⁵¹ Where a voluntary surrender procedure is lodged, it is applied for by the insolvent or his agent.⁵² Only the high court can grant a sequestration order⁵³ as it affects the status of a natural person.⁵⁴ Once the order is granted, the debtor loses control of the estate which then vests in the master and after his appointment by the master in the trustee.⁵⁵ Generally, civil proceedings relating to the estate and execution of any judgment are stayed until the appointment of a trustee,⁵⁶ while international guidelines suggest that a moratorium on debt enforcement should kick in once the case has been filed.⁵⁷ The appointed trustee fulfils his duties under supervision of the master and in accordance with directions given by creditors.⁵⁸ Creditor participation is accepted in South African law but is not favoured by

⁴⁸ S 9.

⁴⁹ Ch 2 par 2.7.

⁵⁰ S 3.

⁵¹ See par 3.3.2.

⁵² S 3(1). Where the insolvent is deceased or incapable of managing his own affairs the person entrusted with the administration of the estate will apply for the order. S 3(3) provides that the court may direct the petitioner or any other person to appear and be examined before making a decision. Where spouses are married in community of property an application for the surrender of the joint estate should be brought; Matrimonial Property Act 88 of 1984, s 17(4)(a).

⁵³ S 149(1)(a) and (b) read with the definition of ‘Court’ in s 2.

⁵⁴ An insolvent is precluded from holding various offices. He is for instance disqualified from being a member of the national assembly, provincial legislature or municipal council; director of a company; business rescue practitioner; member of certain statutory boards or bodies; liquidator of a company or a close corporation; trustee of an insolvent estate; and liquor manufacturer or distributor; see Boraie and Delpont ‘Effects of sequestration’ 522–523 and authorities cited there. See also s 23(3) of the Insolvency Act that provides that an insolvent may not do business as a trader who is a general dealer or a manufacturer or be in the service of or has an interest in the foregoing without his trustee’s written consent. S 23(2) of the Insolvency Act provides that an insolvent must also obtain written consent from his trustee in the event that he concludes a contract that does or could possibly adversely affect his estate.

⁵⁵ S 20(1)(a).

⁵⁶ S 20(1)(b) and 20(1)(c).

⁵⁷ See ch 2 par 2.7.

⁵⁸ S 81. See Bertelsmann *et al Mars* ch 14 as regards the trustee’s election, appointment and remuneration from which its stringent regulation can be deduced. See also ch 15 on the rights and duties of the trustee.

international guidelines.⁵⁹ The trustee is tasked with the sale of estate assets and the distribution of proceeds to creditors in accordance with the Insolvency Act.⁶⁰ In this regard the group of creditors takes preference to individual creditors as was referred to above. Secured creditors' rights are, in line with international principles and guidelines,⁶¹ protected in that the proceeds of property subject to securities will be used to satisfy their claims, in order of preference, after costs for maintenance, conservation and realisation of the property have been paid.⁶² Where a secured creditor did not solely rely on the proceeds of his security, the unpaid balance of his claim will rank as unsecured.⁶³ The Act provides for the setting aside of impeachable transactions entered into before sequestration which prejudiced a creditor or creditors or which preferred certain creditors to others.⁶⁴ Another effect of a sequestration order on the debtor is that his contractual capacity is limited until he is rehabilitated.⁶⁵ The rehabilitation takes place automatically after a period of ten years,⁶⁶ which is in accordance with international principles and guidelines that favour the reduction in court involvement, although the period is exorbitant.⁶⁷ Rehabilitation can take place earlier on application to the high court.⁶⁸ Debts are only discharged upon rehabilitation.⁶⁹ It should be noted that provisional or final sequestration orders may be rescinded. The reasons for rescission are that the order should not have been granted or that ensuing factors render a rescission or variation necessary or appropriate.⁷⁰

⁵⁹ Ch 2 para 2.6.2.4 and 2.7.

⁶⁰ Ss 82 and 113.

⁶¹ Ch 2 par 2.7.

⁶² Ss 89(1), 89(3) and 95(1). In the event that the free residue is insufficient to satisfy the insolvent's funeral and deathbed expenses, the proceeds of property subject to securities will be used therefor; s 96(4).

⁶³ S 83(12).

⁶⁴ Ss 26, 27, 29, 30, 31 and 34.

⁶⁵ See Bertelsmann *et al Mars* 172–173 and authorities cited there.

⁶⁶ S 127A.

⁶⁷ Ch 2 par 2.7.

⁶⁸ S 124.

⁶⁹ S 129(1)(b).

⁷⁰ See s 149(2) and Bertelsmann *et al Mars* 24–26 and authorities cited there.

Further relating to the administration of a sequestrated estate, as was briefly touched upon above, the master of the high court⁷¹ is tasked with the supervision of the administration of insolvent estates in terms of the Insolvency Act.⁷² Although it is difficult to define its role, it can be said that it is that of a regulator.⁷³

3.3.2 Access requirements and effect thereof

3.3.2.1 General

As indicated above, there are two routes leading to a sequestration order, namely, voluntary surrender and compulsory sequestration. It has also been noted that the access requirements in respect of these two procedures differ and that it is more difficult to obtain an order via the voluntary surrender route, due to the more stringent formal requirements and the higher burden of proof. These aspects are discussed below.

Both substantive and procedural requirements must be complied with before a court may accept an application for the voluntary surrender of an estate. The procedural requirements are as follows:

- a. The debtor must, not more than 30 days but not less than fourteen days before the date upon which the application will be made, publish a notice of surrender in the *Gazette* as well as a newspaper circulating in the district in which he resides or where his principal place of business is situated.⁷⁴
- b. The debtor must, within seven days from date of publication of the notice of surrender in the *Gazette*, deliver or post a copy thereof to every creditor whose address he knows or can ascertain.⁷⁵ A copy of the notice must, within the same period, be furnished by post to every registered trade union that to the debtor's knowledge represents any of his employees. It must

⁷¹ The master of the high court is a 'creature of statute' as it only possesses the powers and has the duties conferred on it by law.

⁷² The master does not oversee the debt review and administration order procedures; see ch 4 par 4.2 and 4.3.

⁷³ Calitz 2011 *De Jure* 297.

⁷⁴ S 4(1). The notice must be in a form that is substantially similar to form A in the first schedule of the Act. According to s 8(f) it is an act of insolvency if the debtor does not proceed with the application after having published a notice of surrender (which has not lapsed or been withdrawn in terms of ss 6 or 7).

⁷⁵ See also *Ex parte Arntzen* 2013 (1) SA 52 (KZP). See Boraie and Roestoff 2014 *THRHR* 367 *et seq* for a discussion of the case.

also be sent to the employees themselves.⁷⁶ A copy must further be posted to the South African Revenue Service.⁷⁷

- c. The debtor must, in duplicate, lodge a statement of affairs at the master's office. Where there is no local master's office in the district where the debtor resides or carries on business, a further copy must be lodged at the office of the magistrate of the district.⁷⁸

The effect of a notice of surrender is that all sales in execution are stayed. However, where the value of the property is less than R5 000 the master, or where it exceeds R5 000 the court, may order the sale of property so attached and direct as to how the proceeds should be applied.⁷⁹ The master may, after the

⁷⁶ This is done by affixing a copy to a notice board to which the employees have access inside the debtor's premises or if there is no access to the premises to the front gate thereof. It can also be affixed to the front door of the premises from which the debtor conducted business immediately prior to the surrender.

⁷⁷ Hereafter the 'SARS'. S 4(2). See also s 197B(1) of the Labour Relations Act 66 of 1995. There are several conflicting decisions dealing with the effect of a defect regarding the notice of surrender and the court's powers in such circumstances with specific reference to s 157(1). S 157(1) provides that

[n]othing done under this Act shall be invalid by reason of a formal defect or irregularity, unless a substantial injustice has been thereby done, which in the opinion of the court cannot be remedied by any order of the court.

See *Lion Match Co Limited v Wessels* 1946 OPD 376; In *Ex parte Oosthuysen* 1995 (2) SA 698 (T) it was held that failure to comply is fatal to the application. In *Ex parte Harmse* 2005 (1) SA 323 (N) 329–330 Magid J disagreed with the decision in *Oosthuysen*. It was held that non-compliance is a formal defect that can be remedied by the court. See also the discussion by Bertelsmann *et al Mars* 51 and Meskin *et al Insolvency law* par 3.3.1. In the latter work the following conclusion is reached:

Accordingly it is submitted that notwithstanding the fact that sections 4(1) and 4(2) are couched in ostensibly peremptory terms, failure in any respect to comply with those provisions is a formal defect, within the meaning of section section [sic] 157(1) since it involves a departure from the relevant prescribed form ... The first question, therefore, is whether the defect has, or may have, caused prejudice, which must be answered in the light of the object of the relevant provisions ... Where the Court finds that it has not, and could not have, caused any prejudice, the defect is validated, without any necessity for the Court to make any order, whether for condonation or otherwise. Where the Court finds that the defect has, or may have caused prejudice, the second question is whether such is capable of being cured by an order of the Court. Such order cannot be an order of 'condonation' but one by which the prejudice may be discounted.

⁷⁸ S 4(3) and (5). The statement of affairs should substantially correspond to form B in the first schedule of the Act. According to *Ex parte Berson* 1938 WLD 113–114 the purpose is to provide every creditor with information regarding the insolvent's property and liabilities as well as the cause of insolvency so that such creditors can draw proper conclusions as to how to proceed. Meskin *et al Insolvency law* par 3.3.2 propose that, in relation to non-compliance, generally the same approach as proposed under s 4(1) and (2) should be followed.

⁷⁹ S 5(1).

notice of surrender has been published, also appoint a *curator bonis* to the debtor's estate.⁸⁰

Subject to the court's discretion,⁸¹ the applicant must in accordance with section 6 satisfy the court, on a balance of probabilities, of four aspects before he will succeed with his application. These are the substantive requirements which entail:⁸²

- a. That the formalities have been complied with;
- b. that the applicant is in fact insolvent,⁸³
- c. that the insolvent owns realisable property of sufficient value to cover all sequestration costs which would be payable out of the free residue; and

⁸⁰ S 5(2).

⁸¹ S 6(1). The exercise of this discretion depends on the relevant circumstances; Meskin *et al Insolvency law* par 3.5. It is also important to note that the court has a further inherent jurisdiction to prevent abuse of process; Meskin *et al Insolvency law* par 2.1.5 and Boraine and Roestoff 2014 *THRHR* 371. See also *Ex Parte Shmukler-Tshiko* in relation to abuse of process, although Boraine and Roestoff note that Satchwell J's view that sequestration applications aimed at obtaining relief are, as a matter of course, abusive in nature, blurs the boundaries as regard abuse as clear indications of ulterior motives are necessary to establish same; 371. Regarding the court's discretion in applications for voluntary surrender Gorven J in *Ex parte Arntzen* par 58 n22 stated that he could not find any authority on the point. However, he referred to the decision of Wallis J in *FirstRand Bank Ltd v Evans* 2011 (4) SA 597 (KZD) regarding a provisional order relating to an application for compulsory sequestration where Wallis J stated that the discretion involves power and duty (with reference to *Schwartz v Schwartz* 1984 (4) SA 467 (A) 473H-474E which was approved in *South African Police Service v Public Servants' Association* 2007 (3) SA 521 (CC) par 17). Gorven J also referred to and quoted from *FirstRand Bank Ltd v Evans* 607 where it was stated that

[i]n other words, where the conditions prescribed for the grant of a provisional order of sequestration are satisfied, then, in the absence of some special circumstances, the court should ordinarily grant the order. It is for the respondent to establish the special or unusual circumstances that warrant the exercise of the court's discretion in his or her favour.

However, Gorven J submitted that voluntary surrender applications call for a different approach as the debtor is the applicant and not the party opposing the application and further, that a creditor brings the application in compulsory proceedings which indicates the attitude of at least one of the creditors. He notes that a 'more general approach' has been followed in voluntary surrender applications (with reference to *Ex parte van den Berg* 1950 (1) SA 816 (W) 817–818 and *Ex parte Ford & Two Similar Cases* 383) but that no proper consideration was given to the nature of the discretion in these matters.

⁸² See *Ex parte Shmukler-Tshiko* on the importance of proving the substantive requirements. See in general *Ex parte Arntzen* for a discussion of the requirements for voluntary surrender.

⁸³ Insolvency refers to 'actual insolvency' where liabilities actually exceed the value of assets. This is also known as the 'balance sheet test'. See *inter alia Ex Parte Van den Berg* 1962 (4) SA 404 (O); *Ex Parte Harmse* 325; *Ex Parte Shmukler-Tshiko* 10. However, commercial insolvency (relating to liquidity) is included in the concept; Boraine and Delpont 'Introduction' 487. The liquidity test is preferred by the international natural person insolvency community and is easier to apply; ch 2 par 2.7.

d. that sequestration is to the advantage of creditors.⁸⁴

As regards the latter two requirements, international principles and guidelines provide that discrimination, specifically on financial grounds, should be avoided.⁸⁵

The Insolvency Act does not specifically provide for the opposing of a voluntary surrender by creditors in court. However, creditors may oppose the application⁸⁶ by applying for leave to intervene and filing affidavits setting out the grounds of such opposition. If allowed, the matter will be postponed, parties will file affidavits and the case will be set down on the opposed roll.⁸⁷

The 2015 Insolvency Bill⁸⁸ proposes a provisional order where the debtor applies for the liquidation⁸⁹ of his estate.⁹⁰ Another proposed modification is that it requires debtors to provide security for payment of all costs in respect of the application that may be awarded against the applicant as well as costs of the liquidation, which are not recoverable from creditors.⁹¹ The requirement that there should be sufficient free residue to cover sequestration costs has been omitted from the bill as it apparently does not add to the requirement of advantage for creditors⁹² (which is retained)⁹³ and probably also as security will in any event be set. Some of the formal requirements have also been omitted,

⁸⁴ See par 3.3.2.2.

⁸⁵ Ch 2 par 2.7.

⁸⁶ Van Heerden and Boraine argue that the court in *Ex parte Ford* did not attach sufficient weight to the fact that the application was unopposed when exercising its discretion; 2009 *PELJ* 57.

⁸⁷ See Bertelsmann *et al Mars* 69.

⁸⁸ The then South African Law Commission brought out a report titled the *Report on the review of the law of insolvency* in 2000. It contained a draft bill as well as an explanatory memorandum – hence the ‘2000 Insolvency Bill’ and ‘2000 *Explanatory memorandum*’ respectively. The latest versions of these documents are unofficial working copies on file with the author (hereafter ‘Bill’ or ‘2015 Insolvency Bill’ and ‘2014 *Explanatory memorandum*’ respectively). This research mostly refers to the 2015 Insolvency Bill except where it specifically states that the clause referred to is as provided in the 2000 Insolvency Bill.

⁸⁹ The 2015 Insolvency Bill uses the term ‘liquidation’ when referring to both liquidation of juristic persons and sequestration of natural persons and partnerships.

⁹⁰ Cl 3 in general and cl 3(8) specifically read together with cl 10. See also 2014 *Explanatory memorandum* par 3.14.

⁹¹ See cl 3(3)(b) and 2014 *Explanatory memorandum* par 3.4. The debtor should not more than fourteen days prior to the date of the application obtain a certificate from the master confirming that security has been set.

⁹² Cl 3(8) is silent on the matter. See 2014 *Explanatory memorandum* par 3.17.

⁹³ See cl 3(8)(ii), cl 10(1)(c)(i) and cl 11(1)(c) and 2014 *Explanatory memorandum* par 3.15.

such as prior notice to creditors and advertisement.⁹⁴ Clause 3(3) now only requires that a statement of affairs be lodged.⁹⁵ However, other substantial requirements have been added. The first is apparently included to clarify the uncertainty that has emerged in light of the impact of the debt review procedure in terms of the NCA on voluntary surrender applications.⁹⁶ This requirement provides that⁹⁷

an application for debt review in terms of section 86 of the National Credit Act, 2005 (Act No. 34 of 2005) has been concluded or the debtor satisfies the court that such an application would not serve a useful purpose.

Two more references to other procedures, although not direct requirements that the debtor must satisfy, have been added. Even though the Bill does not require debtors to satisfy the court as regards the unsuitability of these procedures, the court may only make an order for sequestration where these procedures are inappropriate. As the matter is brought before the court by means of a motion, the applicant debtor will obviously carry the burden of proof in this regard. Clause 3(8)(a)(iv) provides that the court must make a provisional order only if the following procedures are not more appropriate:

1. Post or pre-liquidation composition in terms of section 118 or 119;
2. Administration order in terms of section 74 of the Magistrates' Courts Act 32 of 1944.⁹⁸

As far as applications for compulsory sequestrations are concerned, one or more of the debtor's creditors, with the required claim(s), may apply for such order.⁹⁹

The formalities are:

- a. That the applicant provides security to the master to defray all sequestration costs until a trustee is appointed;¹⁰⁰ and

⁹⁴ It is proposed that notice to the master, trade unions, employees and the SARS be retained; see cl 3(4).

⁹⁵ See also 2014 *Explanatory memorandum* par 3.1.

⁹⁶ See par 3.3.2.3 as well as ch 4 par 4.3.

⁹⁷ Cl 3(8)(a)(iii) read with cl 10(c)(iii) as well as cl 11(1)(d) and 2014 *Explanatory memorandum* par 3.16.

⁹⁸ Cl 3(8)(a)(iv) read with cl 10(c)(iv) as well as cl 11(1)(e) and 2014 *Explanatory memorandum* par 3.16.

⁹⁹ S 9(1).

¹⁰⁰ S 9(3)(b). The applicant must obtain a certificate from the master, confirming that security was given not more than ten days prior to the application, which certificate must be filed with the application.

- b. that the applicant furnish the debtor, the SARS as well as employees and registered trade unions (where applicable), with copies of the application.¹⁰¹

The court may grant a provisional sequestration order if the applicant can *prima facie* prove:¹⁰²

- a. That he has a liquidated claim of at least R100 against the debtor;¹⁰³
- b. that the debtor has committed an act of insolvency¹⁰⁴ or is in fact insolvent; and
- c. that there is reason to believe that sequestration will be to the advantage of creditors.

In accordance with section 12, the court has a discretion¹⁰⁵ and may order the final sequestration of the debtor's estate if the court is satisfied that:

- a. The creditor has a liquidated claim against the debtor;
- b. the debtor has committed an act of insolvency or is in fact insolvent; and
- c. there is reason to believe that sequestration will be to the advantage of creditors of the estate.

As mentioned earlier, clause 3(3)(b) of the 2015 Insolvency Bill requires a debtor who applies for his own liquidation to provide security. Similarly clause 5(3)(c) proposes that a creditor who applies for a liquidation order should set security for payment of all costs which may be awarded against the applicant and all costs of the liquidation which are not recoverable from creditors of the estate. The commission is of the view that this requirement will discourage applications that

¹⁰¹ S 9(4A).

¹⁰² S 10.

¹⁰³ Where more than one creditor applies jointly they must in aggregate have liquidated claims for R200 or more.

¹⁰⁴ See s 8 regarding the acts of insolvency. In *Madari v Cassim* 1950 (2) SA 38 (N) it was held that the application for an administration order in terms of section 74 of the Magistrates' Court Act qualifies as an act of insolvency in terms of section 8(g); see also ch 4 par 4.2.5. In *Ex parte Shmukler-Tshiko* 6, the court incorrectly accepted that acts of insolvency are also relevant in voluntary surrender applications. The international community considers acts of bankruptcy to be out-dated as the focus should be on the inability to pay and not on wrongful actions by the debtor; WB *Report* 62–63 and ch 2 par 2.7.

¹⁰⁵ See above regarding the court's discretion.

are not to the advantage of creditors and that it will prevent friendly applications.¹⁰⁶ In this regard it states that

[t]here is usually little risk to guarantee the payment of costs if liquidation will clearly be to the advantage of creditors. Cheaper remedies should be pursued if there are insufficient assets to make liquidation worthwhile.¹⁰⁷

It is submitted that the reference to ‘cheaper remedies’ correlates with the added requirement relating to the debt review procedure as well as the references to post or pre-liquidation composition and the administration order procedures as regards voluntary surrender applications. As far as compulsory proceedings are concerned it is submitted that ‘cheaper remedies’ can only refer to a non-friendly creditor utilising individual enforcement proceedings.

At first glance it seems that clauses 10 and 11 of the 2015 Insolvency Bill propose substantially the same burden of proof for provisional and final liquidation orders irrespective of whether the debtor himself or a creditor (or creditors) applies for such order. The only exception is that where a debtor applies he must satisfy the added requirement relating to the debt review procedure in terms of the NCA.¹⁰⁸ However, as clauses 10 and 11 both provide that the requirements of clause 3 (as regards debtors’ applications) and clause 5 (as regards creditors’ applications) must be complied with, debtors will yet again get the shorter end of the stick. This is so as clause 3, amongst others, requires positive proof that liquidation will be to the advantage of creditors,¹⁰⁹ whereas clause 5 is silent on the matter. In contrast, clauses 10 and 11 merely require that there is reason to believe that liquidation will be to the advantage of creditors.¹¹⁰

In line with international trends and best practice, the 2015 Insolvency Bill has done away with acts of insolvency and rather focuses on the inability to pay.¹¹¹

¹⁰⁶ See 2014 *Explanatory memorandum* para 3.5 and 5.14. See par 3.3.2.2 as regards friendly compulsory applications and the controversy surrounding them.

¹⁰⁷ *Idem* par 3.5.

¹⁰⁸ See cl 10(1)(c)(iii) and cl 11(1)(d).

¹⁰⁹ Cl 3(8)(a)(ii).

¹¹⁰ Cl 10(1)(c)(i) and cl 11(1)(c).

¹¹¹ See 2014 *Explanatory memorandum* para 2.3, 2.7 and 2.8 as well as cl 2.

This development is to be welcomed. However, some remnants of section 8(b)¹¹² are still present as similar circumstances qualify as ‘unable to pay’ in terms of the Bill.¹¹³ Furthermore, an omission by the debtor to act upon a statutory demand for payment or security, or to enter into a compromise as regards outstanding debt also qualifies as such.¹¹⁴ This begs the question whether the legislature are truly attempting to do away with acts of insolvency or whether comments in the 2014 *Explanatory memorandum* merely pay lip service to such intentions whilst new ‘acts of insolvency’ are almost secretly brought into the fold of what is to be considered as being ‘unable to pay’.

3.3.2.2 Advantage for creditors requirement

As was demonstrated above, sections 6, 10 and 12 of the Insolvency Act contain the prerequisite that the applicant in an application for a sequestration order should show that either it will be (in the case of a voluntary surrender application)¹¹⁵ or there is reason to believe that it will be (in case of a compulsory sequestration application)¹¹⁶ to the advantage of the debtor’s creditors if his estate is sequestrated.¹¹⁷ As far as this requirement is concerned, Smith explains as follows:¹¹⁸

In considering the provisions of the Act it becomes apparent that there is a recurrent motif or dominant thread (if ‘thread’ is used in the sense of something that runs a continuous course through anything) and that is the advantage of creditors, not one creditor, or some creditors but the creditors as an entity or the *concursum creditorum*.¹¹⁹

¹¹² S 8(b) provides that a debtor commits an act of insolvency if a court has given judgment against him and he fails, upon the demand of the officer whose duty it is to execute that judgment, to satisfy it or to indicate to that officer disposable property sufficient to satisfy it, or if it appears from the return made by that officer that he has not found sufficient disposable property to satisfy the judgment.

¹¹³ See cl 2(2)(b) and 2014 *Explanatory memorandum* para 2.2 and 2.13.

¹¹⁴ See cl 2(2)(a) and 2014 *Explanatory memorandum* 2.9.

¹¹⁵ S 6(1).

¹¹⁶ Ss 10(c) and 12(c).

¹¹⁷ This requirement is central to the South African Insolvency Act and has been part of South African insolvency legislation since 1916. See ss 10 and 12 of the Insolvency Act 32 of 1916. For a thorough discussion of the advantage for creditors requirement see Roestoff *in Kritiese evaluasie* 347 *et seq*; Swart *Rol van ’n concursum creditorum* 273 *et seq* and Smith 1985 *MB* 27.

¹¹⁸ Smith 1985 *MB* 28.

¹¹⁹ Smith refers to various sections in the Act that do not specifically use the phrase ‘advantage to creditors’ but are designed for the benefit of creditors; *idem* 28 *et seq* and ss 13, 16, 19, 20, 21, 23, 26, 29, 30, 31, 65, 69, 119 and 152. As regards the Insolvency Acts’ emphasis on increasing payment to creditors, Borraine and Roestoff refer to the *WB Report* and submit that lawmakers should also take cognisance of the social benefits of an effective insolvency

Footnote continues on next page

In the recent case of *Ex parte Ford*, the applicants averred that they had a 'constitutional right' to the acceptance of the surrender of their estates.¹²⁰ However, the court confirmed that the primary object of the voluntary surrender procedure is not the relief of harassed debtors.¹²¹ With reference to the decision of the Supreme Court of Appeal in *Nel NO v Body Corporate of the Seaways Building*¹²² it held that the purpose of the Insolvency Act is not the deprivation of creditors' claims but merely the regulation of the manner and extent of their payments.

A remark by Bertelsmann J in *Ex parte Ogunlaja*¹²³ in the context of voluntary surrender applications reflects the predicament in which debtors find themselves. He remarked that

[u]nless and until the Insolvency Act is amended, the South African insolvency law requires an advantage to creditors before the estate of an individual can be sequestrated. Much as the troubled economic times might engender sympathy for debtors whose financial burden has become too much to bear, the insolvency law seeks to protect the interests of creditors at least to the extent that a minimum advantage must be ensured for the concurrent creditor when the hand of the law is laid on the insolvent estate.

Although the phrase 'advantage to creditors' is not defined or further explained in the Act, case law shows that it entails a reasonable prospect of some pecuniary benefit accruing to the general body of creditors.¹²⁴ Roper J in *Meskin v Friedman* put it as follows:¹²⁵

In my opinion, the facts put before the Court must satisfy it that there is a reasonable prospect – not necessarily a likelihood, but a prospect which is not too remote – that some pecuniary benefit will result to creditors.

system which include the removal of the social costs of leaving debtors in a state of on-going distress and the benefit of enabling debtors to become productive for both their own benefit and that of society; Boraine and Roestoff 2014 *THRHR* 543.

¹²⁰ 383.

¹²¹ With reference to *Ex parte Pillay*.

¹²² 1996 (1) SA 138 (A).

¹²³ [2011] JOL 27029 (GNP) par 36.

¹²⁴ See *Meskin & Co v Friedman* 1948 (2) SA 559 (W); *London Estates (Pty) Ltd v Nair* 1957 (3) SA 591 (D); *BP Southern Africa (Pty) Ltd v Furstenburg* 1966 (1) SA 720 (O); *Lynn & Main Inc v Naidoo* 2006 (1) SA 69 (N) and *Ex parte Bouwer* 2009 (6) SA 386 (GNP); see also *Meskin et al Insolvency law* para 2.1.4 and 3.2.

¹²⁵ 559.

In this regard Smith submits that the ‘indirect advantages’¹²⁶ that the sequestration procedure provides cannot on their own satisfy the advantage for creditors requirement as the majority of cases show that there should still be a reasonable prospect of some pecuniary benefit for creditors.¹²⁷ What would constitute a reasonable dividend depends on the circumstances of each case and the attitude of creditors.¹²⁸ However, the practical implementation of the advantage for creditors requirement is problematic as even the best estimates at the time of application will not be accurate as the available funds for distribution will only be ascertained once the assets have been liquidated. The efficacy of this requirement can thus be questioned.¹²⁹

Because sequestration proceedings ultimately lead to a discharge of debt, coupled with the fact that the formalities and burden of proof are more stringent in the case of voluntary surrender proceedings than in the case of compulsory sequestration,¹³⁰ a tendency has developed where debtors request friends or family members to bring an application for their compulsory sequestration.¹³¹ These applications have suitably been dubbed ‘friendly sequestrations’.¹³² The application is usually based on a written notice by the debtor to his creditor(s)

¹²⁶ Referring to those which are not pecuniary in nature, although they lean towards ‘the ultimate pecuniary advantage of creditors’. These are, amongst others, the right of inquisition and the control of and power to dispose of assets.

¹²⁷ Smith 1985 *MB* 32. See also *Meskin & Co v Friedman* 559; *London Estates (Pty) Ltd v Nair* 592; *BP Southern Africa (Pty) Ltd v Furstenburg* 720 as referred to by Smith and also *Roestoff ’n Kritiese evaluasie* 348 and *Swart Rol van ’n Concursum creditorum* 275.

¹²⁸ *Roestoff ’n Kritiese evaluasie* 348. See also *Trust Wholesalers and Woollens (Pty) Ltd v Mackan* 1954 (2) SA 109 (N); *Fesi v ABSA Bank Ltd* 2000 (1) SA 499 (C). In *Nieuwenhuizen v Nedcor Bank Ltd* [2002] 2 All SA 367 (O), 10 cents in the rand were accepted as a point of departure in the determination of whether the advantage for creditors requirement was met. See the discussion of the case by O’Brien and Boraïne 2001 *SAILR* 1. More recently in *Ex parte Ogunlaja* par 9 the court found, with reference to the practice rule in the North Gauteng high court, Pretoria that at least 20 cents in the rand were required to show advantage for creditors.

¹²⁹ See Boraïne 2003 *De Jure* 227–228.

¹³⁰ Voluntary surrender requires positive proof of advantage for creditors where compulsory sequestration requires only a ‘reasonable prospect’ that it will be to the advantage of creditors. See par 3.3.2.1 above and compare the wording of ss 10(c) and 12(1)(c). See also Smith 1981 *MB* 59; Smith 1997 *JBL* 50 and Evans 2001 *SA Merc LJ* 490 *et seq.*

¹³¹ See for example *Esterhuizen v Swanepoel* 2004 (4) SA 89 (W). See also in general Smith 1997 *JBL* 50 and Evans 2001 *SA Merc LJ* 485.

¹³² See in general Bertelsmann *et al Mars* 98 and 138 as well as *Meskin et al Insolvency law* par 2.1.5.

that he is not able to pay his debt – which qualifies as an act of insolvency.¹³³

Conradie J summarised the characteristics of friendly sequestrations as follows:¹³⁴

Friendly sequestrations seem to share certain characteristics. Although, like pornography, they may be hard to define, they are easy to recognize. The debt which the sequestrating creditor relies upon is almost always a loan. It is usually quite a small loan, very often made in circumstances where it would have been apparent to the whole world that the respondent was in serious financial difficulty. Despite this, the loan is customarily made without security of any sort. It is seldom evidenced by a written agreement, or even subsequently recorded in writing. The only writing that is produced to the court is the letter stating, with appropriate expressions of dismay that the debt cannot be paid, and, sometimes, for good measure, setting out details of the respondent's assets and liabilities. Very often debtor and creditor are related: fathers commonly sequester sons, wives sequester husbands and sweethearts sequester each other, without, I am sure, any damaging effect on their relationship.

Such applications run the risk of being classified as procedural abuse as there is a risk of collusion¹³⁵ between the applicant and the debtor where information is deliberately withheld from the court.¹³⁶ Even though a friendly application is not necessarily 'wrong',¹³⁷ it is wrong where other creditors' interests are infringed and especially when there is deception.¹³⁸ However, it will be in order where there is no indication of abuse and where the evidence complies with the requirements of section 12 of the Act.¹³⁹ Nevertheless, courts have called for the practice in relation to friendly sequestrations to be tightened and emphasised the need to scrutinise these applications and to curb abuse of procedure to assure that there will be advantage for creditors.¹⁴⁰ Some judgments even went so far as

¹³³ See par 3.3.2.1 and s 8(g) as well as *Mthimkhulu v Rampersad* [2000] 3 All SA 512 (N). For a discussion of the case see Evans 2001 SA Merc LJ 489 *et seq*.

¹³⁴ *Craggs v Dedekind* 1996 (1) SA 937 (C).

¹³⁵ *Idem* 937. In *Esterhuizen v Swanepoel* Satchwell J examined some of the 'hallmarks' of collusive applications; 91 *et seq*. See also *Shmukler-Tshiko 7 et seq* where Satchwell J took a harsh stand towards friendly applications.

¹³⁶ For a discussion of the abuse of process and the courts' reaction there to see Evans 2001 SA Merc LJ 492 *et seq*.

¹³⁷ See *Beinash & Co v Nathan* 1998 (3) SA 541 (W) and the discussion of the case by Smith 1998 JBL 157. See also *Esterhuizen v Swanepoel* 91.

¹³⁸ Smith 1997 JBL 50.

¹³⁹ See *Beinash & Co v Nathan*, which referred to *Kerbel v Chames* 1925 WLD; *Wepener v Erickson* 1926 WLD and *Yenson & Co v Garlick* 1926 WLD 57.

¹⁴⁰ See in this regard, amongst others, *Hillhouse v Stott*; *Freban Investments (Pty) Ltd v Itzkin*; *Botha v Botha* 1990 (4) SA 580 (W); *Craggs v Dedekind* 937 *et seq*; *Ex parte Steenkamp*

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to set guidelines and additional requirements in friendly applications.¹⁴¹ Others declined to do so as it infringes on the functions of the legislature and the notion that each case must be decided on its own facts and circumstances — especially since sequestration orders rely on the discretion of the courts which must be unfettered.¹⁴²

Although friendly sequestrations can sometimes be seen as an abuse of process,¹⁴³ it may be asked whether this phenomenon is not a sign that South African insolvency law has fallen behind the times due to, amongst others, the ‘advantage for creditors’ requirement which makes it extremely difficult for the man in the street to apply for a voluntary surrender in order to rid himself of excessive debt.¹⁴⁴ In this regard Roestoff acknowledges Flemming J’s insight in *Sellwell Shop Interiors* where he remarked that insolvency legislation might have fallen behind modern times and merits a reconsideration as far as advantage for creditors are required in all cases.¹⁴⁵ However, Roestoff submits that the answer to the problem does not lie in the mere abolition of the advantage requirement, as credit providers’ interests must still be protected. She is nevertheless critical of cases where additional requirements for friendly sequestrations were set as it is not the task of the courts to amend the Act.¹⁴⁶

1996 (3) SA 822 (W); *Streicher v Viljoen* [1999] 3 All SA 257 (NC); *Van Rooyen v Van Rooyen* [2000] 2 All SA 485 (SE); *Mthimkhulu v Rampersad*; and *Esterhuizen v Swanepoel*. For a discussion of *Hillhouse v Stott* see Evans and Haskins 1990 SA Merc LJ 246. However, it is only necessary to critically consider evidence where cooperation is evident; see *Beinash & Co v Nathan* 542. See also the discussion in Roestoff *’n Kritiese evaluasie* 358.

¹⁴¹ I.e. *Beinash & Co v Nathan* 542 *et seq*; *Meyer v Batten* 1999 (1) SA 1041 (W) and *Mthimkhulu v Rampersad* 517.

¹⁴² *Hillhouse v Stott* 586. See also *Sellwell Shop Interiors v Van der Merwe* unreported case number 27527/90 (W) as discussed by Roestoff *’n Kritiese evaluasie* 364–366.

¹⁴³ *Meskin et al Insolvency law* par 2.1.5.

¹⁴⁴ See Borraine and Roestoff 1993 *De Jure* 230–236; Borraine and Roestoff 2000 *Obiter* (Part 2) 261–263; Evans 2001 SA Merc LJ 485 and Roestoff *’n Kritiese evaluasie* 431. As will be seen from the discussion in chapter 4, secondary statutory debt relief measures do not necessarily provide an answer to those who do not qualify for the voluntary surrender procedure.

¹⁴⁵ Roestoff *’n Kritiese evaluasie* 365–366.

¹⁴⁶ *Idem* 388–389.

In recent times, the courts have also become stricter when it comes to voluntary surrender applications. In *Ex parte Mattysen et Uxor*¹⁴⁷ it was stated that the essence of ‘advantage for creditors’ is that the court must make a decision, on the evidence presented, that there are sufficient assets in the estate (with sufficient value) to pay the costs of sequestration and a not-negligible dividend to creditors.¹⁴⁸ In this regard courts have of late demanded more precise information relating to the debtor’s affairs as well as a realistic calculation of the potential dividend.¹⁴⁹ Bertelsmann J explained the reason for this rigorous approach as follows:¹⁵⁰

The requirement that all information presented to the court in an application for surrender must be accurate and that the valuations must be exact arises from the courts’ insistence that a debtor who is pressed by his creditors does not over-estimate the value of his estate in order to obtain relief from his financial burdens. The administration of insolvent estates has over the years developed into a very lucrative and therefore competitive profession. The pressure has therefore increased to identify debtors whose sequestration or liquidation may render a lucrative return to lawyers, trustees, liquidators, valuers and auctioneers. Advertisements in the media canvassing debtors who are desirous of ridding them of their financial burdens have become commonplace. This has increased the risks for debtors and creditors alike. Debtors who might be able to meet their obligations if they were given the opportunity to properly arrange their affairs, are pressurised into opting for insolvency proceedings instead, often if not always losing their homes and motor vehicles as a result thereof, suffering the consequences of a bad credit record for many years thereafter. On the other hand, insolvency practitioners are tempted to present a rosy picture of the debtor’s affairs that bears little semblance to reality, resulting in an estate being declared insolvent that renders little or no dividend for creditors once the fees of the various participants in voluntary surrender proceedings have been deducted and the administration costs have been paid.¹⁵¹

In *Ex parte Mattysen* the court dismissed the application for voluntary surrender as the applicant did not provide a proper basis for calculating the dividend. He

¹⁴⁷ 2003 (2) SA 308 (T). See also *Ex Parte Arntzen (Nedbank Ltd intervening)* 2013 (1) SA 49 (KZP).

¹⁴⁸ *Ex parte Mattysen* 316.

¹⁴⁹ See in general *Ex parte Boucher*.

¹⁵⁰ Bertelsmann *et al Mars* 63 quoted with approval in *Ex parte Boucher* 384.

¹⁵¹ See also *Ex parte Mattysen* where Southwood J inferred that the deliberate misrepresentation of the facts was made with the assistance of the applicants’ attorney. The judge referred the matter to the law society to investigate the attorney’s conduct in the preparation and presentation of the matter.

could therefore not prove that the surrender would be to the advantage of his creditors. It was further evident that the valuator did not have personal knowledge of the facts and that the valuation of assets came down to ‘a bald statement which is not supported by any facts or reasons’.¹⁵² In *Ex parte Ogunlaja* the court set out the necessary evidence that a valuator should provide in order to establish ‘benefit to creditors’. These include detail as to the valuator’s engagement with the asset, detailed descriptions of the property as well as when and how the comparable sales method should be used.¹⁵³

The recent matter of *Ex Parte Arntzen* perhaps best illustrates the courts’ frustration with voluntary surrender applications. In this case two of the substantive requirements, namely, realisable property of sufficient value to cover all costs of sequestration from free residue as well as the advantage requirement were under consideration. With reference to case law,¹⁵⁴ the court stated that ‘full and frank disclosure’ is necessary in voluntary surrender applications due to, amongst others, the stringent test set out in section 6(1) and the fact that it is brought on an *ex parte* basis which requires the utmost good faith.¹⁵⁵ According to the court, full and frank disclosure is very important within the realm of voluntary surrender applications as they are brought on an *ex parte* basis whilst not truly being *ex parte* in nature. This is because other persons or entities, for example creditors, have an interest in the matter. Even though creditors are notified of the application,¹⁵⁶ they do not receive the same benefits as they would have had, had they been cited as respondents. The court stated that creditors in these circumstances have to be ‘more alert, proactive and must respond more quickly in assessing whether or not to intervene’. This is so as creditors need to examine the statement of affairs and if insufficient information is provided therein, an inspection of the application itself is necessary, all within a limited time frame. The court noted that many credit providers do not have the resources to

¹⁵² *Ex parte Mattysen* 314.

¹⁵³ Para 18–33.

¹⁵⁴ See *Ex parte Swart* 1935 NPD 433; *Berrange NO v Hassan* 2009 (2) SA 339 (N) 354A–B as referred to by the court; 51.

¹⁵⁵ The court referred to *Schlesinger v Schlesinger* 1979 (4) SA 342 (W) 349A–C and *Phillips v National Director of Public Prosecutions* 2003 (6) SA 51 (SCA).

¹⁵⁶ See s 4.

‘routinely and timeously’ follow up on such notices and even where they follow up, they may reach the conclusion that it is not worthwhile to intervene in the matter – especially where small estates are at stake. In such instances the prospect of recovering legal costs is slim, even where the application is successful. The court was thus of the opinion that creditors are ‘peculiarly vulnerable to voluntary surrender applications which, at a superficial level, make out a case that sequestration is inevitable’. It continued that in such instances an overburdened court may also not examine the application as properly as it would if it were opposed – and in doing so may not detect material non-disclosures. Another reason supporting the call for ‘a higher level of disclosure’ is that the process does not require a two-stage approach, as is the case in compulsory sequestration applications, where provision is made for a provisional and a final order.¹⁵⁷

The court referred to the position of a decade ago when various divisions of the high court tightened their approach to friendly sequestration applications which proliferated at the time. It referred to and quoted extensively from *Mthimkhulu* which described the tendency as a ‘cottage industry’¹⁵⁸ and stated that in many cases there was ‘a very grave suspicion of collusion’¹⁵⁹ which led to practice guidelines being laid down in the Natal division of the high court.¹⁶⁰ Full and frank disclosure coupled with clear proof of the necessary facts were required. Generally, documentary proof of the indebtedness that founded the applicant’s *locus standi* and a complete list of the insolvent’s assets were obligatory. This included a valuation by a qualified person stating convincing reasons for the valuation that was made of movable and immovable property. In *Mthimkhulu* it was also noted that the claimed value of household furniture and effects as well as second-hand motor vehicles (which are frequently relied upon to show advantage for creditors) regularly do not correspond to their true value.¹⁶¹

¹⁵⁷ Proposals in the 2015 Insolvency Bill will negate this concern as both the proposed provisions in relation to security and a provisional order will probably form part of voluntary surrender applications in future; par 3.3.2.1.

¹⁵⁸ *Mthimkhulu v Rampersad* 514 and 516.

¹⁵⁹ *Idem* 516.

¹⁶⁰ *Idem* 517.

¹⁶¹ *Ex parte Arntzen* 53 and *Mthimkhulu v Rampersad* 517.

Again referring to and quoting from *Mthimkhulu* the court noted that reference was made to the number of cases where a final sequestration order was made but that

the friendly creditor makes no effort to have a trustee appointed or to prove his claim, no creditor takes steps to prove a claim because of a fear of contribution, the debtor waits for the dust to settle and with his old creditors off his back carries on business as normal.¹⁶²

It was noted that in such instances the sequestration of the estate is not to the advantage of creditors and that such applications come down to an abuse of the court process, which undermines creditors' rights. The court observed that only the debtor benefits at the expense of his creditors.¹⁶³

Gorven J was of the opinion that voluntary surrender applications, as was the case with friendly sequestration applications a decade ago, had begun to proliferate in the Kwazulu-Natal high court. The court observed that '[a] fledgling cottage industry has reared its head' and that many of these applications were drafted by the same attorneys who made use of a standard form with similar averments. The court noted that in most instances small estates were involved. It took cognisance of an innovative method to satisfy the requirements that the costs of sequestration must be defrayed from the estate and that advantage for creditors must be shown. This entails that a friend or relative undertakes to pay the attorney's fees and that the attorney will not turn to the estate for outstanding costs.¹⁶⁴

The court concluded that in voluntary surrender applications 'there is an even greater risk of abuse and a risk that the interests of creditors will be undermined' than in friendly applications. According to the court, this emphasises the necessity for full and frank disclosure as well as proper evidence as to the debtor's estate. Some additional reasons that the court laid down in favour of a more stringent approach in voluntary surrender applications are that applicants seem to concentrate on the section 4 requirements and do not appear to grasp

¹⁶² *Mthimkhulu v Rampersad* 514.

¹⁶³ *Ex parte Arntzen* 53.

¹⁶⁴ *Idem* 53–54.

the seriousness of the more onerous requirement of ‘advantage for creditors’. Secondly, in *ex parte* applications the courts inevitably have to trust the founding papers. Thirdly, unlike the case in friendly applications, no collusion is necessary since the applicant is the debtor with a direct interest in the matter.¹⁶⁵

The court therefore found it a fitting starting point to require compliance with the guidelines as provided in *Mthimkhulu* also in voluntary surrender applications. It held that where documents are available that will support averments made, such documents should be provided. Further, courts should require admissible evidence in support of these applications rather than rely on ‘bare averments’ or unsupported valuations that are not corroborated by affidavits, convincing reasoning or relevant qualifications. The court quoted a *dictum* from Conradie J in *Craggs*, namely, that ‘a Court should be forgiven for requiring rather more ... [in making out a case] ... than it might otherwise do’.¹⁶⁶

Again quoting from *Craggs*, the court stated that an applicant ‘should present sufficiently detailed evidence to satisfy a sceptical Court’¹⁶⁷ that the requirements of section 6(1) have been met and that a court should subsequently grant the order. The court concluded its reasoning with the well-known passage from Holmes J in *Ex parte Pillay*¹⁶⁸ that ‘[t]he machinery of voluntary surrender was primarily designed for the benefit of creditors, and not for the relief of harassed debtors’.¹⁶⁹

In light of the principles set out above, Gorven J had various problems with the founding affidavit in the case before him. He found that even if the factual disputes between the intervening creditor and the applicant were ignored, the application was lacking in various respects. Some of these inadequacies were that the valuation of immovable property concerned was based on a mere letter unsupported by an affidavit by the person who valued the property. There was no reference to comparable sales, no description of improvements or whether

¹⁶⁵ *Idem* 54.

¹⁶⁶ *Craggs v Dedekind* 937.

¹⁶⁷ *Idem* 937.

¹⁶⁸ 311.

¹⁶⁹ *Ex parte Arntzen* 54–55.

the valuation was based on market value or a forced sale. The valuation of a motorcycle was also not adequate as it was based on a letter without indicating the reason why the valuator qualified as an expert. It was unsupported by an affidavit and no reason for the value was provided.¹⁷⁰ The amount relating to the costs of sequestration also reflected a mere averment without any basis for such conclusion. After the costs were challenged by Nedbank, the applicant indicated that a friend would settle the costs as a gift and that it would not be claimed from the estate. Another serious deficiency was that the founding affidavit stated that demands were issued by certain creditors without naming them. In reply, the debtor disclosed for the first time that he was under the debt review procedure in terms of the NCA without providing further information thereof¹⁷¹ which clearly had a serious bearing on the matter.¹⁷²

However, even if the court disregarded the debt review process, it noted that an important factor in considering the requirement of ‘benefit for creditors’ is whether ‘the indebtedness is likely to be liquidated over time if the income of the applicant exceeds expenses’. The court remarked that disclosure relating to income and expenditure is of special importance in small estates or where there is a moderate difference in value between the assets and liabilities. Further, it referred to the possibility of a trustee making use of section 23(5) of the Act in terms of which a trustee is entitled to such money that (in the opinion of the master) is not necessary for the maintenance of the debtor or his dependants. Unfortunately, according to the court, the application also failed dismally in providing sufficient information regarding the debtor’s income and expenditure.¹⁷³

The court held that the applicant had failed to satisfy the court that he owned realisable property of sufficient value to defray all costs of the sequestration application. The court was also not satisfied that a sequestration order would be

¹⁷⁰ *Idem* 55–56.

¹⁷¹ See ch 4 par 4.3.

¹⁷² *Ex parte Arntzen* 56–57.

¹⁷³ *Idem* 57–58.

to the benefit of creditors. The application was therefore dismissed and the applicant was directed to pay the costs of Nedbank's intervention.¹⁷⁴

It is clear from the discussion above that it is mostly the advantage requirement that restricts a debtor's access to the sequestration procedure as a form of debt relief and, as was stated above, that a South African debtor can be 'too broke to go bankrupt'.¹⁷⁵ Without commenting on the prudence of recent calls for and by the courts to increase the scrutiny of voluntary surrender applications, as well as the additional requirements and guidelines that were set, it is clear that it will be even more difficult for natural person debtors to obtain sequestration orders in future.

As can be seen from the proposed reform discussed in paragraph 3.3.2.1, the Law Reform Commission is in favour of the retention of the advantage for creditors requirement.¹⁷⁶ The commission acknowledges the criticism against the requirement and that it is not common in other systems. However, it argues for its retention by stating that¹⁷⁷

it is unacceptable to use the expensive procedure of liquidation by the court in cases where the value of the assets is insufficient to ensure a benefit to creditors.

The commission is of the opinion that the proposed clause 118 procedure would assist debtors where advantage for creditors cannot be proved.¹⁷⁸

3.3.2.3 Effect of secondary statutory debt relief measures on voluntary surrender applications

It has already been shown that South African natural person insolvents have three statutory debt relief measures at their disposal, the primary one being the sequestration procedure as discussed above.¹⁷⁹ The two secondary remedies,

¹⁷⁴ *Idem* 58–59.

¹⁷⁵ Rochelle 1996 *TSAR* 319.

¹⁷⁶ See cl 3(8)(a)(ii), cl 10(1)(c)(i) and cl 11(1)(c).

¹⁷⁷ 2014 *Explanatory memorandum* par 3.15.

¹⁷⁸ *Ibid.* See ch 5 par 5.2 as regards the proposed pre-liquidation composition.

¹⁷⁹ See par 3.3.2.1 and ch 1 par 1.1.

namely, the administration order¹⁸⁰ and the debt review¹⁸¹ procedures are regulated by section 74 of the Magistrates' Courts Act¹⁸² and section 86 of the NCA respectively. The question thus arises as to how the different statutory procedures impact on one another and for purposes of the discussion in this chapter specifically, how the two secondary measures impact on sequestration proceedings.¹⁸³

Section 74R of the Magistrates' Courts Act provides that an administration order is not a bar to a sequestration order. The statutory provision is therefore clear and there is no uncertainty regarding the effect of the administration order procedure as a secondary debt relief procedure on the primary natural person debt relief procedure, namely, the sequestration procedure. On the other hand, the effect of a sequestration order is so far-reaching that it would be both impractical and impossible to obtain an administration order after an estate has already been sequestrated.¹⁸⁴ However, save for one minor issue, the interplay between the debt review procedure and sequestration proceedings is not addressed by either the NCA or the Insolvency Act. The question is thus whether the NCA excludes the application of the Insolvency Act where credit agreements, as regulated by the NCA, are under consideration.¹⁸⁵ Van Heerden and Boraine note that the reason for this question is that section 3 of the NCA places emphasis on the satisfaction of all responsible financial obligations¹⁸⁶ and section 2(1) provides that the 'Act must be interpreted in a manner that gives effect to the purposes set out in section 3'. However, section 2(7) provides that the Act is not to be construed to limit, amend, repeal or otherwise alter any other piece of legislation. Further, schedule 1 of the NCA entitled 'Rules concerning conflicting legislation' does not mention the Insolvency Act and there is no direct reference to the latter Act in any provision of the NCA. Nevertheless, the NCA did consider

¹⁸⁰ See ch 4 par 4.2.

¹⁸¹ See ch 4 par 4.3.

¹⁸² 32 of 1944.

¹⁸³ The other side of the coin, namely, the impact of sequestration proceedings on the secondary statutory measures is discussed in ch 4 para 4.2.5 and 4.3.3.

¹⁸⁴ See Joubert 1956 *THRHR* 140.

¹⁸⁵ The NCA only applies to credit agreements as defined by the Act; see ch 4 par 4.3.1.

¹⁸⁶ See ss 3(c)(i), 3(g) and 3(i) below.

the Insolvency Act as schedule 2 prescribes amendments to the latter,¹⁸⁷ although they do not have a bearing on the interplay between the two procedures under consideration.¹⁸⁸ Furthermore, it is interesting to note that, notwithstanding the controversy that can be detected in judgments, the legislature did not consider the interplay between the two procedures when the NCA was amended in 2015 – save for a minor amendment in this regard. This amendment was effected in terms of the National Credit Amendment Act,¹⁸⁹ which became effective on 13 March 2015. The schedule to the Amendment Act inserts section 8A into the Insolvency Act, which reads as follows: ‘A debtor who has applied for a debt review must not be regarded as having committed an Act of insolvency.’¹⁹⁰

On the basis of the above, except for the development in terms of the Amendment Act, Van Heerden and Borraine submit that the NCA does not oust (directly or by necessary implication) the application of the Insolvency Act.¹⁹¹ They further submit that a construction in terms of which a pending debt review, restructuring order or agreement in terms of the NCA constitutes a bar to sequestration ‘can lead to absurdity’ and state that such a conclusion may result in unequal treatment of both credit providers and debtors.¹⁹²

Therefore, although clarity has been provided in that an application for the debt review procedure does not result in an act of insolvency, the exact impact of the debt review procedure on insolvency proceedings is not clear. This matter was

¹⁸⁷ S 84 of the Insolvency Act is amended as follows:

(a) the substitution for the heading of the following heading:

‘Special provisions in case of goods delivered to a debtor in terms of an instalment agreement’; and

(b) the substitution for the opening clause of subsection (1) of the following words:

‘If any property was delivered to a person (hereinafter referred to as the debtor) under transaction that is an instalment agreement contemplated in paragraph (a), (b), and

(c)(i) of the definition of ‘instalment agreement’ set out in section 1 of the National Credit Act, 2005.’

Section 84 of the Insolvency Act grants the creditor a hypothec over property whereby the outstanding amount is secured.

¹⁸⁸ See Van Heerden and Borraine 2009 *PELJ* 36–37 where they discuss the provisions referred to above.

¹⁸⁹ 19 of 2014 (hereafter ‘Amendment Act’).

¹⁹⁰ See the schedule to the Amendment Act. This matter is discussed further in ch 4 par 4.3.

¹⁹¹ Van Heerden and Borraine 2009 *PELJ* 36 *et seq.*

¹⁹² *Ibid.*

considered in *Ex parte Ford*¹⁹³ where three unopposed applications for voluntary surrender were decided by Binns-Ward J. It was apparent from all three applications that a considerable portion of the applicants' debts arose from credit agreements as contemplated by the NCA. Furthermore, the magnitude of the debts was disproportionately high in relation to the debtors' incomes. It was stated in the applications that the applicants had 'become insolvent by misfortune and due to circumstances beyond [their] control, without fraud or dishonesty on [their] part'.¹⁹⁴ The court suspected that credit was recklessly granted¹⁹⁵ and mentioned that one of the objects of the NCA is to discourage such behaviour.¹⁹⁶ In this context, the judgment referred to various phrases and sections in the NCA¹⁹⁷ which are repeated here to reflect the proper context of the case even though these aspects of the NCA are only thoroughly discussed in chapter 5.¹⁹⁸ The judgment firstly referred to some parts of the NCA's long title which explain the aim of the Act as follows:

[T]o promote a fair and non-discriminatory marketplace for access to consumer credit and for that purpose, amongst other matters, to promote responsible credit-granting *and* use, and for that purpose to prohibit reckless credit-granting and to provide for debt reorganisation in cases of over-indebtedness.

The court also referred to the purposes of the Act as set out in section 3 and quoted from the section as follows:

The purposes of this Act are to promote and advance the social and economic welfare of South Africans, promote a fair, transparent, competitive, sustainable, responsible, efficient, effective and accessible credit market and industry, and to protect consumers, by –

...

- (c) promoting responsibility in the credit market by –
 - (i) encouraging responsible borrowing, avoidance of over-indebtedness and fulfilment of financial obligations by consumers; and
 - (ii) discouraging reckless credit granting by credit providers and

¹⁹³ For discussions of the case see Van Heerden and Borraine *PELJ* 2009 22 and Borraine and Van Heerden 2010 *PELJ* 84.

¹⁹⁴ *Ex parte Ford* 378.

¹⁹⁵ As regards reckless credit see Vessio 2009 *TSAR* 272; Stoop 2009 *SA Merc LJ* 365; and Van Heerden 'Over-indebtedness and reckless credit' 11.4.

¹⁹⁶ *Ex parte Ford* 379.

¹⁹⁷ *Ex parte Ford* 379–381.

¹⁹⁸ See ch 5 par 5.5.

contractual default by consumers;

...

- (g) addressing and preventing over-indebtedness of consumers, and providing mechanisms for resolving over-indebtedness based on the principle of satisfaction by the consumer of all responsible financial obligations;

...

- (i) providing for a consistent and harmonised system of debt restructuring, enforcement and judgement, which places priority on the eventual satisfaction of all responsible consumer obligations under credit agreements.

Sections 80 and 81 were subsequently considered as they specifically describe what would constitute reckless credit and what a credit provider should do to prevent itself from extending such credit. Section 80(1) provides as follows:

A credit agreement is reckless if, at the time that the agreement was made, or at the time when the amount approved in terms of the agreement is increased, other than an increase in terms of section 119(4) –

- (a) the credit provider failed to conduct an assessment as required by section 81(2), irrespective of what the outcome of such an assessment might have concluded at the time; or
- (b) the credit provider, having conducted an assessment as required by section 81(2), entered into the credit agreement with the consumer despite the fact that the preponderance of information available to the credit provider indicated that –
 - (i) the consumer did not generally understand or appreciate the consumer's risks, costs or obligations under the proposed credit agreement; or
 - (ii) entering into that credit agreement would make the consumer over-indebted.

Section 81(2) and (3) provides that

- (2) A credit provider must not enter into a credit agreement without first taking reasonable steps to assess –
 - (a) the proposed consumer's –
 - (i) general understanding and appreciation of the risks and costs of the proposed credit, and of the rights and obligations of a consumer under a credit agreement;
 - (ii) debt re-payment history as a consumer under credit agreements;
 - (iii) existing financial means, prospects and obligations; and
 - (b) whether there is a reasonable basis to conclude that any commercial purpose may prove to be successful, if the consumer has such a purpose for applying for that credit agreement.
- (3) A credit provider must not enter into a reckless credit agreement with a prospective consumer.

Section 85 of the Act serves as the basis for the court's consequent decision and provides as follows:

- Despite any provision of law or agreement to the contrary, in any court proceedings in which a credit agreement is being considered, if it is alleged that the consumer under a credit agreement is over-indebted, the court may
- (a) refer the matter directly to a debt counsellor with a request that the debt counsellor evaluate the consumer's circumstances and make a recommendation to the court in terms of section 86(7); or
 - (b) declare that the consumer is over-indebted, as determined in accordance with this Part, and make any order contemplated in section 87 to relieve the consumer's over-indebtedness.

The court also considered sections 86¹⁹⁹ and 87²⁰⁰ of the NCA and stated that a debt counsellor on request by a court in terms of section 85 can recommend to a magistrate's court to declare some of the credit agreements to be reckless. Section 83 sets out the orders that a court (and now also the National Consumer Tribunal)²⁰¹ can make when an agreement was found to be reckless, which includes the setting aside of all or some of the consumer's rights and obligations and to suspend the force and effect of the agreements.²⁰²

The court considered the question why the mechanisms contained in the NCA would not be more suited to the applicants' circumstances than the 'blunter instruments afforded in terms of the voluntary-surrender remedy under the Insolvency Act'. It held that the language used in section 85 is cast in very wide terms and that it is not restricted to credit agreements where debt enforcement has commenced. It also held that the provision of section 4 of the Insolvency Act requires full disclosure of an applicant's proprietary position.²⁰³ In this regard the court referred to the advantage for creditors requirement regarding which the applicant must satisfy the court. This would, in instances where over-

¹⁹⁹ The 'Application for debt review'.

²⁰⁰ Containing the powers of the magistrates' courts to re-arrange a consumer's obligations.

²⁰¹ See s 25 of the Amendment Act.

²⁰² *Ex parte Ford* 380. Boraine and Van Heerden note that the court did not consider its discretion to deal directly with the presumably reckless credit agreements as it is allowed to do in terms of s 83(1) which at the time provided that despite any law or contract to the contrary a court, in any court proceedings where a credit agreement is considered, has the power to declare any such agreement to be reckless in accordance with ch 4 pt D; Boraine and Van Heerden 2010 *PELJ* 96 n72. S 83(1) was subsequently amended by the Amendment Act, but the amendment does not have a bearing on the present discussion.

²⁰³ With reference to Bertelsmann *et al Mars* par 3.15.

indebtedness arose from credit agreements, according to the court, necessitate the consideration of the existence and effect of such agreements. It remarked that the fact that the NCA did not generally alter the Insolvency Act acknowledges that insolvency can arise in a variety of circumstances, which may be unrelated to over-indebtedness resulting from credit agreements as contemplated by the NCA. However, the court noted that where insolvents' misfortune arises from credit agreements they would be well advised to consider the policy, objects and remedies of the NCA before utilising the mechanism of voluntary surrender. It held that the NCA 'provides a wide range of remedial relief which can be tailored to the justice of the particular case' which varies from disallowance of the recovery of the debt, to a stay in the accrual of interest and the ranking of liability. Nevertheless, none of the three applications before the court properly considered the debt review procedure, beyond it being an administered debt collection. More specifically, the applications did not consider the possibility of reckless credit having been extended.²⁰⁴

As the applicants resisted the relief in terms of section 85, the court did not refer the matter to a debt counsellor for investigation but noted that the applicants were free to utilise the mechanisms of the NCA on their own initiative. The court held that it could not exercise its discretion to accept the voluntary surrender applications as the applicants failed properly to explain why the credit agreements would not be administered more appropriately under the NCA for their own advantage as well as the advantage of responsible credit providers as opposed to those who acted recklessly. The court held that, in the exercise of its discretion, it considered the lack of explanation as to the circumstances under which the applicants were able to obtain credit to the extent demonstrated in the applications and why the applicants did not avail themselves of the NCA's remedies. Further, the demonstrated pecuniary advantage to creditors was marginal. It held that an insolvent is not free to choose the form of debt relief 'simply by mechanically and superficially satisfying the relevant statutory requirements under the Insolvency Act' especially where the remedy as 'chosen'

²⁰⁴ *Ex parte Ford* 381–382.

by the insolvent is discretionary.²⁰⁵ It was held that the court had a duty, in the exercise of its discretion, to give proper regard and effect to the public policy in the NCA and that this policy prefers the rights of responsible credit providers to reckless credit providers, and full satisfaction of 'all responsible financial obligations' where possible. It was reiterated that the primary object of voluntary surrender is not the relief of harassed debtors²⁰⁶ and that there is a consonance between the objects of the Insolvency Act and the NCA not to deprive creditors of claims but to merely regulate the manner and extent of payment.²⁰⁷ As the court was left with the impression that the NCA constituted the more appropriate mechanism, all three applications were dismissed.²⁰⁸

Boraine and Van Heerden submit that *Ford* did not set the debt review procedure as an additional requirement for voluntary surrender applications, but that a prospective applicant should consider whether such procedure might not be more advantageous and that such a consideration is of key importance when the court exercises its discretion.²⁰⁹ This point of view is supported. However, even though the debt review procedure is not relevant in all circumstances and will consequently not play a role in all voluntary surrender applications, *Ford* did place a new stumbling block in the way of debtors who wish to use the sequestration process as a form of debt relief in instances where they are party to credit agreements.²¹⁰

²⁰⁵ With reference to *Ex parte Hayes* 1970 (4) SA 94 (NC) 96C. I do not agree with the court's sentiment as the legislature's failure to address the issue leaves debtors to decide which procedure would be best in their circumstances, which is something that they are not generally equipped to do. Furthermore, the most recent international guidelines, as contained in the *WB Report*, prefer that such decision should be left to disinterested public agencies; see ch 2 para 2.6.2.1, 2.6.2.5 and 2.7.

²⁰⁶ With reference to *Ex parte Pillay* 311.

²⁰⁷ *Ex parte Ford* 383, with reference to *Nel v Body Corporate of the Seaways Building* 138.

²⁰⁸ *Ex parte Ford* 384. Boraine and Van Heerden are critical of the fact that the court did not give due consideration to the absence of opposition. They submit that sequestration proceedings are expensive and time consuming and that where the applications are turned down the estate will be depleted even further. They pose the question as to why credit providers did not oppose as they probably had considerable information relating to the debtors' financial positions to their disposal. It is also not clear whether the debt review procedure would have yielded a solution at all; Van Heerden and Boraine 2009 *PELJ* 57 and Boraine and Van Heerden 2010 *PELJ* 116.

²⁰⁹ See Van Heerden and Boraine 2009 *PELJ* 51 *et seq* and 56 as well as Boraine and Van Heerden 2010 *PELJ* 112–113.

²¹⁰ Roestoff and Coetzee 2012 *SA Merc LJ* 62. See also Maghembe *A proposed discharge* 164.

Regarding the court's contention that the provisions relating to reckless credit may provide the optimal answer, Boraine and Van Heerden²¹¹ are of the view that it will not necessarily provide a permanent solution to the debtor's problems. This is so as even where a debtor's rights and obligations are set aside, the NCA does not specifically provide that a credit agreement that was entered into recklessly is illegal and consequently null and void. The NCA further does not prohibit restoration. As far as a suspension of the reckless credit agreements is concerned, they submit that even though a suspension may afford some relief regarding the payment of finance charges,²¹² the consumer will still be liable for at least the capital amount once the period of suspension has expired.²¹³ The effectiveness of the reckless credit provisions as debt relief measures is therefore questioned.²¹⁴ The criticism expressed by Boraine and Van Heerden is supported. The authors also warn against exercising discretion under section 85 as a 'matter of course' where there is doubt as to the viability of the debt review procedure.²¹⁵

It has already been noted that the 2015 Insolvency Bill proposes that a court may only make a provisional order in voluntary surrender applications if either a debt review application has been concluded or the debtor satisfies the court that such procedure would not serve a useful purpose.²¹⁶ The reform provisions, in contrast with the *Ford* decision, therefore elevate at least a consideration of the

²¹¹ Boraine and Van Heerden 2010 *PELJ* 98.

²¹² S 84(1)(b) provides that:

During the period that the force and effect of a credit agreement is suspended in terms of this Act –

(b) no interest, fee or other charge under the agreement may be charged to the consumer.

²¹³ S 84(2) further provides as follows:

After a suspension of the force and effect of a credit agreement ends –

(a) all the respective rights and obligations of the credit provider and the consumer under that agreement –

(i) are revived; and

(ii) are fully enforceable except to the extent that a court may order otherwise; and

(b) for greater certainty, no amount may be charged to the consumer by the credit provider with respect to any interest, fee or other charge that were unable to be charged during the suspension in terms of subsection (1)(b).

²¹⁴ See ch 5 par 5.5 for a continuation of the discussion of the NCA's reckless credit provisions within the ambit of debt relief.

²¹⁵ Boraine and Van Heerden 2010 *PELJ* 120.

²¹⁶ CI 3(8)(a)(iii) and 2014 *Explanatory memorandum* par 3.16.

debt review procedure (and by implication also the reckless credit provisions) to a separate requirement in voluntary surrender applications.

3.3.3 Excluded or exempted property

An aspect directly linked to the debtor's actual rehabilitation and his ability to make a fresh start is the extent to which the law provides for excluded and/or exempted property.²¹⁷ The policy behind exemption laws also dictates that a debtor's dignity should remain intact and that he should not become a burden to society.²¹⁸ In this paragraph, the assets that are generally excluded from the insolvent estate (and therefore remain vested in the insolvent) and those that are exempted from the estate, although they have initially formed part thereof, are considered. Generally, all of the insolvent's property located in South Africa at the date of sequestration as well as property acquired thereafter, or which may accrue to him during sequestration, form part of the insolvent estate.²¹⁹ However, the Insolvency Act provides that the following property is excluded or exempted from passing to the trustee:²²⁰ (a) Wearing apparel; (b) bedding; (c) household

²¹⁷ WB *Report* 74. See also ch 2 par 2.7. Evans points out that the Insolvency Act's failure to distinguish between excluded and exempted assets creates various problems. The basic difference between the two concepts is that excluded assets should never form part of the insolvent estate whereas exempt assets do initially form part of the estate but are later, for the benefit of the debtor, exempted therefrom; Evans *A critical analysis* 250 and 254. See Evans and Steyn 2014 *PELJ* 2746 as regards the status of property in insolvent estates in general.

²¹⁸ Evans *A critical analysis* 444.

²¹⁹ S 20(2) read with the definition of 'property' in s 2. See Evans *A critical analysis* ch 8 regarding the position of property acquired during sequestration.

²²⁰ For in-depth discussions of excluded and exempted property see Evans *A critical analysis* ch 9. Various other laws also provide for property that does not vest in the trustee. See in general Bertelsmann *et al Mars* 192 *et seq* as well as Evans *A critical analysis* 267 *et seq*. These are, amongst others, benefits accruing to an employee in terms of s 33 of the Unemployment Insurance Act 63 of 2001; compensation under the Compensation for Occupational Injuries and Diseases Act 130 of 1993; benefits to a miner under the Occupational Diseases in Mines and Works Act 78 of 1973; life insurance policies to some extent as provided for in s 63 of the Long-Term Insurance Act 52 of 1998; trust assets in accordance with s 12 of the Trust Property Control Act 57 of 1988; trust property held in the name of a financial institution as trustee as determined by s 4(5) of the Financial Institutions (Protection of Funds) Act 28 of 2001; trust money held by an attorney, notary, conveyancer, sheriff or estate agent in accordance with s 78(7) of the Attorneys Act 53 of 1979, s 32(3) of the Estate Agents Affairs Act 112 of 1976 and s 22(3) of the Sheriff's Act 90 of 1986; a spouse's right to share in accrual as determined in the Matrimonial Property Act 88 of 1984; loans under the Land and Agricultural Development Banks Act 15 of 2002; goods, facilities and property under the National Suppliers Procurement Act 89 of 1970; debts and rights ceded *in securitatem debiti* where it amounts to an absolute session subject to the right to claim re-cession; state-subsidised housing in terms of the Housing Act 107 of 1997; the right of a labour tenant to apply for an award of land or a right in land under the Land Reform Act

Footnote continues on next page

furniture; (d) tools; (e) other essential means of subsistence;²²¹ (f) a moderate sum of money or goods as may be necessary for the debtor and his dependants' support;²²² (g) a fideicommissary's interest in property;²²³ (h) pension as a result of services rendered;²²⁴ (i) compensation for loss or damage as a result of defamation or personal injury;²²⁵ and (j) remuneration or reward for work done or professional services rendered by the insolvent or on his behalf after sequestration.²²⁶

Commentators are critical of the property exclusions and exemptions in the Insolvency Act as they are not based on proper policy considerations and are 'unevenly balanced to favour the creditors'.²²⁷ It is also argued that the exclusions and exemptions appear to be merely perfunctory since they hold limited value for the debtor as they are probably insufficient to support the debtor and his dependants.²²⁸ In this respect, the South African position is in contrast with international guidelines that call for the protection of assets and income that are necessary to secure a decent living standard for the insolvent and his dependants. In this regard international best practice favours a standards-based approach where generally all property is exempted and where the obligation to claim assets of excessive value is placed on the insolvency representative.²²⁹

In clause 14(7)(a) of the 2015 Insolvency Bill, the Law Reform Commission proposes an expansion of excluded property in order to create certainty and to

3 of 1996; and property purchased by the insolvent, that has not been delivered – see Bertelsmann *et al Mars 222 et seq* regarding the effects of sequestration on uncompleted contracts.

²²¹ S 82(6). Items (a)–(e) are subject to creditors' determination or if there are no creditors that have proven claims, determination by the master.

²²² The trustee with the master's consent may prior to the second meeting of creditors allow such exemption; s 79.

²²³ S 2.

²²⁴ S 23(7).

²²⁵ S 23(8).

²²⁶ S 23(9). This provision is subject to s 23(5).

²²⁷ Evans *A critical analysis* 312–313, 433 and 453.

²²⁸ *Idem* 432–433. See also Boraine and Roestoff 2014 *THRHR* 545.

²²⁹ Ch 2 par 2.7.

bring it in line with section 39 of the Supreme Court Act²³⁰ and section 67 of the Magistrates' Courts Act.²³¹ The proposed exclusions are as follows:

- (i) The necessary beds, bedding and wearing apparel;
- (ii) the necessary furniture (other than beds) and household utensils of the insolvent in so far as they do not exceed the amount of R2,000 or the amount prescribed from time to time so as to reflect subsequent fluctuation in value of money;
- (iii) stock, tools and agricultural implements of a farmer, in so far as they do not exceed R2,000 in value or the amount prescribed from time to time so as to reflect subsequent fluctuation in the value of money;
- (iv) the supply of food and drink in the house sufficient for the needs of the insolvent and his or her family during one month;
- (v) tools and implements of trade, in so far as they do not exceed the amount or (sic) R2,000 or the amount prescribed from time to time so as to reflect subsequent fluctuation in the value of money;
- (vi) professional books, documents or instruments necessarily used by the insolvent in his or her profession, in so far as they do not exceed the amount of R2,000 or the amount prescribed from time to time so as to reflect subsequent fluctuation in the value of money;
- (vii) such arms and ammunition as the insolvent is required by law, regulation or disciplinary order to have in his or her possession as part of his or her equipment; and
- (viii) necessary medicine and medical devices.

Clause 45(4)(k) provides that the liquidator, if authorised by the master or creditors, has the power to make a sum of money or assets available to the insolvent for his maintenance as well as that of his dependants.²³² Clause 45(4)(l) similarly provides that the liquidator can make assets in excess of the values referred to in clause 14(7) or fixed in terms of clause 14(8) available to the debtor.²³³ Clause 45(6) determines that a liquidator or debtor who is not satisfied with the assets made available by creditors' resolution can refer the matter to the master.²³⁴

²³⁰ 59 of 1959.

²³¹ 2014 *Explanatory memorandum* par 14.4. Such harmonisation is to be welcomed; see also Evans *A critical analysis* 445.

²³² See also 2014 *Explanatory memorandum* par 45.12.

²³³ *Idem* 14.5. As regards the reference to cl 14(8), such a clause does not exist. However, cl 62(4)(l) of the 2000 Insolvency Bill is akin to cl 45(4)(l) of the 2015 Insolvency Bill and referred to cl 11(7) which provided that the minister may change the maximum amounts prescribed.

²³⁴ See also 2014 *Explanatory memorandum* par 14.5.

As regards after-acquired property, the present position is that movable and immovable property, acquired with money in relation to work done or professional services rendered after sequestration of the estate, vest in the insolvent.²³⁵ However, the trustee may claim it for the benefit of the estate.²³⁶ In contrast, clause 14(7)(b) of the 2015 Insolvency Bill proposes that such assets should in future automatically form part of the insolvent estate. This is subject to clause 16 which is headed 'Rights and obligations of debtor during insolvency'. Clause 16(2) provides that a debtor may collect for his own benefit remuneration for work done or payment for professional services rendered by him or on his behalf after the issuing of the liquidation order. However, clause 16(6) sets out a procedure that a liquidator may follow to bring a debtor before a magistrate (in chambers) to supply proof of assets or income received by the debtor as well as estimated expenses for his own support and that of his dependants.²³⁷ The magistrate must issue a certificate stating the portion of the debtor's future earnings that is not required for support and which must accrue to his insolvent estate.²³⁸ Property obtained with earnings which do not, in terms of the certificate, accrue to the insolvent estate, will not form part thereof.²³⁹

Clause 16(5) determines that benefits in terms of pension law or rules of a fund (that is paid after date of liquidation) as well as social benefits do not form part of the insolvent estate.²⁴⁰ This is also the case with compensation by reason of defamation or personal injury, which the debtor may recover for his own benefit.²⁴¹ The exclusion of social grants is in line with international best practice.²⁴²

Evans is critical of the proposed exclusions and submits that the commission's approach to assets is totally devoid of any policy considerations and brings about

²³⁵ See s 23(9). See also *Ex parte Fowler* 1937 TPD 353 and *Ex parte Van Rensburg* 1946 OPD 64.

²³⁶ S 23(5) and 23(11). See in general the discussion in Bertelsmann *et al Mars* 200 *et seq.*

²³⁷ This procedure is to some extent similar to the s 65 procedure contained in the Magistrates' Court Act.

²³⁸ CI 16(6)(e).

²³⁹ CI 16(6)(g).

²⁴⁰ There is no similar provision in the present legislation.

²⁴¹ CI 16(9)(c) and 2014 *Explanatory memorandum* par 16.12.

²⁴² See ch 2 par 2.6.2.5.

minimal change. He is also critical of the low maximum values placed on excluded assets and states that the fact that a motor vehicle does not qualify for exemption essentially renders all other exemptions worthless. He also submits that an express provision should have been included, in line with the fresh-start philosophy, to prohibit a waiver of the right to such property. Furthermore, problems may arise where the minister fails to revise amounts and in this regard it is proposed that the Bill should provide for its compulsory revision, for example every two years.²⁴³

Insolvency legislation does not at present provide for the family home.²⁴⁴ This is so despite the fact that in 1994 South Africa entered a new constitutional dispensation with one of the fundamental rights guaranteed (by the Bill of Rights) being the right to access to adequate housing.²⁴⁵ Section 26(3) also has a bearing on housing and provides for the right not to be evicted from one's home without a court order that was granted after a consideration of all relevant circumstances. Also important is section 28(1)(c) which relates to the rights of children and, within this particular context, specifically the right to shelter.²⁴⁶ No South African judgment has thus far considered the constitutional impact of the attachment and sale of an insolvent's home by the trustee of an insolvent estate in terms of the Insolvency Act,²⁴⁷ although there have been developments regarding these aspects in individual enforcement procedures.²⁴⁸ It is strange that, in light of the express acknowledgment of the right to access to adequate housing in the Constitution and the reform that it brought about in individual enforcement procedures,²⁴⁹ the Law Reform Commission did not consider the impact thereof on insolvency legislation as both the 2000 and 2015 Insolvency Bills as well as the 2014 *Explanatory memorandum* are silent on the matter.

²⁴³ See Evans *A critical analysis* 443 *et seq.*

²⁴⁴ See Steyn 2013 *Int Insolv Rev* 144 and 146.

²⁴⁵ See s 26(1) of the Constitution.

²⁴⁶ A thorough exposition of how, in light of the Constitution, an insolvent's home should be dealt with in insolvency proceedings falls outside the scope of this thesis. In this regard see Evans *A critical analysis* 412 *et seq.* and Steyn *Statutory regulation* 114 *et seq.*; 341 *et seq.*; 407 *et seq.* and 559 *et seq.* See also Steyn 2013 *Int Insolv Rev* 144.

²⁴⁷ See Steyn 2012 *De Jure* 648 and 2013 *Int Insolv Rev* 144 and 146.

²⁴⁸ See *Jaftha v Schoeman* 2005 (2) SA 140 (CC); *Standard Bank of South Africa Ltd v Saunderson* 2006 (2) SA 264 (SCA); *ABSA Bank Ltd v Ntsane* 2007 (3) SA 554 (T); and *Gundwana v Steko Development* 2011 (3) SA 608 (CC).

²⁴⁹ See Steyn 2013 *Int Insolv Rev* 162–164.

Steyn considered the effect of the constitutional imperatives on developments in individual enforcement procedures and came to the following conclusion in relation to insolvency law.²⁵⁰

In the circumstances, it is submitted that legislative intervention is required to provide, in all applications for the sequestration of a debtor's estate, for judicial consideration of 'all the relevant circumstances' pertaining to the home of the insolvent. It is hoped that, in any new insolvency statute, clear policies will be formulated and applied in determining the nature and level of exemptions to be permitted in order to uphold the constitutional rights, including housing and children's rights, of the insolvent and his family. Logistically, any exemption of the home or of any of the proceeds of its sale would impact on, and could be justifiable on the basis of, the ultimate level of discharge for the insolvent.

In concluding the discussion of excluded and exempted property, mention must be made of Roestoff's evaluation of the Law Reform Commission's proposals in light of natural person debt relief specifically. In line with some of the sentiments expressed above, she argues that the proposals are conservative from a debtor's point of view as they only provide the debtor with a very basic standard of living. On the basis that the proposal of a vehicle exemption was rejected outright by credit providers and that the exclusion of a home was not even considered by the Law Reform Commission, she concludes that the South African society's pro-creditor approach is also reflected in the realm of excluded property.²⁵¹

3.3.4 Rehabilitation

It has been mentioned that the sequestration procedure constitutes the primary debt relief procedure in South Africa as it is the only statutory mechanism whereby a debtor can secure a discharge of pre-sequestration debt – and thereby a fresh start.²⁵² However, the discharge is not a guarantee and is only one of the effects of the debtor's rehabilitation.²⁵³

The Insolvency Act provides for rehabilitation through the passage of time²⁵⁴ or

²⁵⁰ Steyn *Statutory regulation* 411. See also Steyn 2013 *Int Insolv Rev* 144.

²⁵¹ Roestoff *n Kritiese evaluasie* 370.

²⁵² See s 129(1)(b). See also par 3.3.1 and ch 1 par 1.1.

²⁵³ See the discussion below.

²⁵⁴ S 127A.

on application to the high court.²⁵⁵ If an insolvent does not apply for his rehabilitation before such time, he will be automatically rehabilitated after a period of ten years from the date of his sequestration.²⁵⁶ However, a court may order otherwise on application by an interested person.²⁵⁷ If an insolvent wishes to be rehabilitated before expiry of the ten-year period, he can bring an application for his rehabilitation by means of the motion procedure.²⁵⁸ The decision to grant such motion is within the court's wide discretion.²⁵⁹ The procedure basically entails that the insolvent must at least three weeks prior to his application furnish security in the amount of R500 for the costs of opposition.²⁶⁰ Interested parties may oppose the application.²⁶¹ The court may grant the rehabilitation order subject to any conditions it sees fit.²⁶² The application for rehabilitation should be brought in accordance with section 124 and the periods and grounds for rehabilitation are as follows:

- a. After twelve months from confirmation of the first trustee's account by the master unless the matter falls within the provisions of paragraph (b) or (c) below.²⁶³
- b. After three years from confirmation of the first trustee's account by the master if the insolvent's estate has previously been sequestrated unless the matter falls within the provisions of paragraph (c) below.²⁶⁴
- c. After five years after the insolvent's conviction of any fraudulent acts relating to the insolvency under consideration or a previous insolvency or of any offence under sections 132, 133 or 134 of the Insolvency Act or any

²⁵⁵ S 124. As a person's status is affected by a rehabilitation order, only the high court can grant such order; see the definition of 'court' in s 2.

²⁵⁶ In the case of a compulsory sequestration the ten-year period commences on the day that the provisional sequestration order was granted; see *Grevler v Landsdown* 1991 (3) SA 178 (T).

²⁵⁷ S 127A(1). Although international principles and guidelines do not refer to any period that must expire before a discharge is granted in asset liquidation proceedings, they propose a period of between three and five years as regards repayment plan or rehabilitation proceedings; ch 2 par 2.7.

²⁵⁸ S 126 sets out the facts that should be averred in an application for rehabilitation. See *Meskin et al Insolvency law* par 14.3 and *Bertelsmann et al Mars* 561 *et seq* for elaborate discussions of procedural aspects.

²⁵⁹ *Ex parte Hittersay* 1974 (4) SA 328 (SWA).

²⁶⁰ S 125.

²⁶¹ S 127(1).

²⁶² S 127(2) and 127(3).

²⁶³ S 124(2)(a).

²⁶⁴ S 124(2)(b).

corresponding provision under the 1916 Insolvency Act.²⁶⁵ Furthermore, the proviso to section 124(2) provides that an insolvent may only, within a period of four years, apply for a rehabilitation order under the above circumstances (a – c) where it has been recommended by the master.²⁶⁶

- d. After six months after the sequestration where no claims have been proven against the estate, where the insolvent has not been convicted of an offence as stated in paragraph (c) above and the insolvent's estate has not previously been sequestrated.²⁶⁷
- e. At any time after the master has confirmed the distribution account where all claims have been paid in full with interest as well as the costs of sequestration.²⁶⁸
- f. Immediately where creditors have agreed to a composition, as envisaged in section 119(7), which resulted in the master having issued a certificate to that effect and provided that the certificate shows that payment has been made or security has been set for payment of at least 50 cents in the rand of every claim proved or to be proven.²⁶⁹

Rehabilitation concludes the sequestration proceedings and discharges the debts of the insolvent.²⁷⁰ It further relieves the insolvent of every disability as a consequence of sequestration.²⁷¹ Generally, rehabilitation does not revert the

²⁶⁵ S 124(2)(c). Prior notice of at least six weeks should be given to the master and the trustee in writing and by advertisement in the *Gazette* as far as items a–c are concerned.

²⁶⁶ In the calculation of the four year period the date of the application to court is used as a starting point; *Ex parte Nathan* 1944 CPD 13.

²⁶⁷ The application must be brought with at least six weeks' notice to the master and the trustee in writing and by publishing a notice in the *Gazette*; s 124(3).

²⁶⁸ The application must be brought with at least three weeks' notice in writing to the master and the trustee; s 124(5).

²⁶⁹ The application should be brought with at least three weeks' notice in the *Gazette* and the said notice should be delivered or posted in a registered letter to the trustee; s 124(1). S 124(4) provides that in all of the above cases, except where the application is made after creditors have been paid in full, a trustee who received a notice as mentioned shall report to the master any facts which would justify the court's refusal, postponement or qualification of the rehabilitation. S 127(1) provides that the master must in all circumstances report to the court on the day of the hearing.

²⁷⁰ Which were due, or had arisen, prior to sequestration, and which did not arise out of any fraud on the insolvent's part. This is in line with international guidelines that favour a wide discharge; ch 2 par 2.7.

²⁷¹ S 129(1).

insolvent with his estate.²⁷² Where all debts have not been paid and there are still assets under control of the trustee, such assets must be realised and distributed²⁷³ as rehabilitation does not affect the right of the trustee or creditors to a part of the estate which is vested in the trustee but has not been distributed. In the unlikely event that surplus funds were paid over to the master (who kept it in the guardians' fund) it should be paid to the insolvent (upon request) after his rehabilitation.²⁷⁴ However, rehabilitation does not have any effect on the insolvent's sureties or on any aspect or person relating to a compromise. Rehabilitation further does not have an effect on the liability of a person to pay a penalty or 'suffer any punishment' under the Act.²⁷⁵

For purposes of this discussion the discharge of debt is the most pertinent aspect relating to rehabilitation. In *Dicks v Pote*²⁷⁶ it was held that a discharge does not have the effect of extinguishing all pre-sequestration debt and that it only renders it unenforceable. However, Bertelsmann *et al* point out that this conclusion was reached with reference to section 120 of Ordinance 6 of 1843 where the words 'discharge the insolvent' were used in contrast with the wording of section 129(1)(b) of the Insolvency Act, namely, 'discharging all debts'. Bertelsmann *et al* are consequently of the opinion that the wording of the Insolvency Act is indicative of another intention, namely, to extinguish pre-sequestration debt and thereby to afford the debtor a complete discharge.²⁷⁷

Section 127(2) makes it clear that a court's powers in relation to rehabilitation are discretionary. It provides that, irrespective of whether the application is opposed, the court may refuse the application, postpone the hearing or rehabilitate the

²⁷² An exception is a rehabilitation granted on application under circumstances as described in s 124(3), for instance where no creditor has proven a claim.

²⁷³ S 129(3)(c) read with s 25(1).

²⁷⁴ S 116(1).

²⁷⁵ S 129(3).

²⁷⁶ 3 EDC 81 and 85. See Roestoff *'n Kritiese evaluasie* 381 who submits that the *Dicks* case is authority that the principle of reaffirmation, as found in American law, is recognised in South African insolvency law. A reaffirmation agreement is one where a debtor promises to pay a debt irrespective of the fact that a discharge has been provided; see Sommer *Consumer bankruptcy* 109.

²⁷⁷ Bertelsmann *et al Mars* 591 n417.

insolvent on any condition.²⁷⁸ Therefore, the insolvent does not have a right to his rehabilitation.²⁷⁹ Meskin *et al* submit that a wide discretion is afforded to the court to accommodate the interests of the insolvent and also those of creditors, the State, the public and specifically the commercial public.²⁸⁰ The essential enquiry is whether, on the facts and accommodating all relevant interests, the insolvent ought to be rehabilitated as a person who should be allowed to participate in commercial activities on the same basis as any other honest person. This depends on how the insolvent conducted his trade before he became insolvent and also on his probable future behaviour in this regard.²⁸¹ It is thus clear that a debtor's good faith is important in the exercise of the court's discretion. A debtor who wishes to obtain an order for rehabilitation should therefore include sufficient information in his application to show that he has learnt a lesson from his insolvency and that he appreciates the possibility that his sequestration could have prejudiced his creditors.²⁸²

The Law Reform Commission proposes a simplification of the provisions of section 124 and is also in favour of a number of other changes to the rehabilitation procedure. Clause 101(1) provides for the following grounds and periods regarding an application²⁸³ for rehabilitation:

²⁷⁸ See *Ex parte Snooke* 2014 (5) SA 443 (FB) where an unopposed application for rehabilitation was postponed, as the court was of the opinion that creditors needed to (once again) be invited to prove their claims at a special meeting.

²⁷⁹ See *Ex parte Hittersay* 1974 (4) SA 328 (SWA) and *Ex parte Fourie* [2008] 4 All SA 340 (D). In the latter case the court (at par 39) stated that 'frankness and a full disclosure of all relevant facts' are required.

²⁸⁰ Meskin *et al* *Insolvency law* par 14.4.1.

²⁸¹ *Ibid* and Bertelsmann *et al Mars* 575 and authorities cited there. See, amongst others, *Ex parte Heydenreich* 1917 TPD 658–659; *Ex parte Le Roux* 1996 (2) SA 423 (C); *Ex parte Van Zyl* 1997 (2) SA 441 (E); *Greub v The Master* 1999 (1) SA 746 (C) 752–753; and *Ex parte Fourie*. Contrary to the international trend to destigmatise natural person insolvency law, South Africa still views insolvents as being somewhat dishonest in general; see ch 2 par 2.7.

²⁸² *Ex parte Le Roux* 424.

²⁸³ Cl 101(8)–(10) is similar to s 126 and sets out the facts that should be averred in an application for rehabilitation. However, the proposed clause adds the phrase 'and his or her own as well as his or her spouse's contribution to his or her household'. The Law Reform Commission quotes from *Ex Parte Palmer and Palmer* 1961 (1) SA 603 (W) where the principle that a husband and wife should according to their means contribute towards the support of the marriage was endorsed; 2014 *Explanatory memorandum* par 101.8. The quote is a passage by De Wet J in the following terms:

It seems to me that a Court considering an application for rehabilitation will usually consider whether the means of the applicant are such that he should be ordered to make a further payment for the benefit of his creditors. In considering this question it is clearly relevant to consider the whole of the income accruing to the household. To take a simple

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- (a) [A]t any time after the confirmation by the Master of a distribution account providing for the full payment of all claims proved against the estate, with interest thereon from the date of liquidation, calculated in terms of section 84(12) and (13) and all costs of liquidation; or
- (b) at any time after the Master has issued a certificate of acceptance of a composition as contemplated in section 119; or
- (c) in any other case after the expiration of four years from the date of the confirmation by the Master of the first liquidation account in the estate.²⁸⁴

A debtor may request the master to recommend that an application on the grounds referred to in clause 101(1)(c) may be made before the four-year period expires. However, such application would not be possible before a period of twelve months has elapsed or where it is not the first time that the debtor's estate is liquidated, before a period of three years has expired.²⁸⁵

example, if the wife and the children are self-supporting, the husband's income is required only for his own support, and it follows that if some income accrues to other members of the family the drain on the husband's income is *pro tanto* reduced.

²⁸⁴ In case of an application that resorts under cl 101(1)(a), the debtor should send a notice of the intended application to the master and the liquidator at least four weeks prior to the date of the application and in the case of an application in terms of cl 101(1)(b), (c) or (d) to the master and liquidator at least six weeks prior to the application date as well as through publication in the *Gazette*. Under the last mentioned circumstances, a copy of the notice should also be forwarded to all known creditors; cl 101(4) (The clause refers to an application in terms of cl 101(1)(d), although the 2015 Insolvency Bill does not contain such a subsection). The novel provision as regards notice to creditors is apparently an attempt to counter 'secret' rehabilitations; 2014 *Explanatory memorandum* par 101.5. The notice must state the estimated value and should state full details of assets at the time of the application; cl 101(6). The rationale behind this initiative is that it would prevent creditors from being surprised by the rehabilitation whilst investigating possible assets. It will further ensure that a creditor has the opportunity to oppose the application for rehabilitation; see 2014 *Explanatory memorandum* par 101.7. This initiative is contrary to international principles and guidelines that suggest that creditor participation should as a matter of course be eliminated; ch 2 par 2.7. Cl 101(4)(b) provides that a debtor should furnish security in the amount of R5 000 to the registrar in order to make provision for a possible cost order against him. Cl 101(5) provides that the minister may amend the amount in line with fluctuations in the value of money. In contrast with s 127(1), where the master had to report to the court on the day of the hearing, cl 102(1)(a) now provides that

[t]he Master must report to the court on the merits of the application and furnish a copy of the report to the applicant or the applicant's attorney.

The Law Reform Commission is of the opinion that the provision, as it currently stands, is impractical and that it is advisable to inform the applicant as soon as possible of the content of the report in order to clarify ambiguities. It is also suggested that an applicant, on the strength of the master's report, may even decide to withdraw the application; 2014 *Explanatory memorandum* par 102.1.

²⁸⁵ Cl 101(3).

The Decriminalisation Act²⁸⁶ spurred a process to rid the South African legal system of unnecessary statutory offences that do not belong in the criminal courts. Therefore, it is proposed that some ‘technical’ offences should be replaced by alternative sanctions. In line with this movement, clause 102(2) provides that if a master’s certificate shows, or there is other evidence that a debtor ‘has intentionally impeded, obstructed or delayed the administration of the insolvent estate’ on the various grounds set out in the clause,²⁸⁷ the insolvent will only be eligible for rehabilitation after a period of ten years.²⁸⁸ However, where a debtor has been convicted of an offence relating to his existing or any prior insolvency, as referred to in section 136(1)(a), (b), (d), (e) or (g)²⁸⁹ or 2(e) or

²⁸⁶ 107 of 1991.

²⁸⁷ These grounds are:

- (a) [F]ailing to submit a statement of affairs in accordance with the requirements of the Act; or
- (b) failing to make available to the liquidator of the estate, in accordance with written directives by the liquidator or the Master, property belonging to the insolvent estate which was in his or her possession or custody or under his or her control or any book, document or record relating to his or her affairs which was in his or her possession or custody or under his or her control; or
- (c) failing to notify the liquidator of the estate of the existence of any book, document, or record relating to his or her affairs which was not in his or her possession or custody or under his or her control, and as to where such book, document, or record could be found, or of any property belonging to his or her insolvent estate which was not mentioned in his or her statement of affairs, and as to where such property could be found; or
- (d) failing to keep the liquidator of the estate informed of any change of his or her address during the period of three years after the liquidation of his or her estate; or
- (e) failing to comply with section 16(3); or
- (f) means of any other act or omission.

²⁸⁸ See also 2014 *Explanatory memorandum* par 102.2. A commentator proposed that the ten-year period should not be peremptory and that the court should have some discretion in this regard, especially since there will be various degrees of culpability. However, the Law Reform Commission is of the opinion that there should be a ‘real danger’ of penalisation and that a wide discretion is therefore not desirable; 2014 *Explanatory memorandum* par 102.4.

²⁸⁹ CI 136(1) provides that:

A debtor or the management of a debtor is guilty of an offence if he or she-

- (a) conceals or parts with or intentionally destroys any book or accounting record relating to the affairs of the debtor or intentionally erases the information contained therein or makes it illegible or permits any other person to perform any such act with regard to any such book or accounting record; or
- (b) alienates property, obtained by him or her or the estate on credit and not paid for, otherwise than in the ordinary course of business; or
- (c) ...
- (d) offers or promises to any person a reward in order to procure the acceptance by a creditor of an offer of compromise or to give up any investigation with regard to the estate or to conceal any information in connection therewith or, in the case of a debtor who is a natural person, to induce a creditor not to oppose an application for rehabilitation; or
- (e) at any time within two years before the date of liquidation of his or her estate or the estate of the debtor, with intent to obtain credit or the extension of credit, gave false

Footnote continues on next page

(f)²⁹⁰ or any other fraudulent act, the debtor may only apply for a rehabilitation order after five years from the date of conviction.²⁹¹

An important amendment is the proposal that the period of six months in terms of the existing section 124(3) be extended to four years. The reasoning behind this proposed amendment is that the fact that no claims have been proven may not necessarily be indicative of the debtor's eligibility for an early discharge, but may rather suggest that the debtor has disposed of all his assets and that his creditors are not amenable to possible contribution. Cases where no claims have been proven will thus resort under clause 101(1)(c) with its resultant general four-year period.²⁹² Another proposed amendment is provided for in clause 101(1)(b), namely, that a court has a discretion to rehabilitate an insolvent immediately after a composition has been accepted without the 50-cents limit (or any monetary limit) attached thereto. The commission argues that compositions should be encouraged and that the 50-cents limit is in any event arbitrary. It further submits that there is probably little correlation between the debtor's eligibility for rehabilitation and the percentage paid to creditors.²⁹³ This correlates with international principles and guidelines in that discrimination on financial grounds ought to be avoided.²⁹⁴

information or concealed any material fact in connection with his or her or the debtor's assets and liabilities to anyone who became his or her or the debtor's creditor.

- ²⁹⁰ CI 136(2) provides that any person is guilty of an offence where he
- (e) receives any benefit or accepts any promise of a benefit as a reward for keeping or undertaking to keep in abeyance or stopping or undertaking to stop any action for the liquidation or inquiry connected with the liquidation of the estate of the debtor or for agreeing or undertaking to agree to a composition or rehabilitation or for not opposing or agreeing not to oppose it for concealing or undertaking to conceal particulars of a debtor or an insolvent estate; or
 - (f) conceals, parts with, damages, destroys, alienates or otherwise disposes of property attached in terms of section 25 or property belonging to the debtor or his or her insolvent estate with intent to frustrate the attachment of such property by virtue of a liquidation order, in terms of section 25, or with intent to prejudice creditors of the insolvent estate.

²⁹¹ CI 101(2). See also 2014 *Explanatory memorandum* par 101.3.

²⁹² 2014 *Explanatory memorandum* par 101.4.

²⁹³ *Ibid.*

²⁹⁴ Ch 2 par 2.7.

The arbitrary period of ten years before an automatic rehabilitation occurs, is retained in the 2015 Insolvency Bill due to its simplicity, the lack of comments received in this regard and because it is relatively well-known.²⁹⁵

The proposed effects of rehabilitation are basically the same as those provided for by the existing Act. However, it is proposed that the ambit of section 129(1)(b) be extended to include some offences. According to clause 104(1)(b), debts that have arisen out of fraud on the insolvent's part or the commission of an offence referred to in clauses 136(1)(c)²⁹⁶ and 136(1)(e)²⁹⁷ in respect of a prior liquidation will not be discharged.²⁹⁸ Further, clause 104(3) provides that evidence of a conviction of an offence as provided for in clause 104(1)(b) is admissible in civil proceedings as *prima facie* evidence of the commission of such an offence.²⁹⁹ Another amendment relating to the effects of sequestration is that the proposed legislation does not provide that the insolvent will be reinvested with his estate where no claims against the estate were proved within six months following sequestration.³⁰⁰ However, clause 98(1) and (2) determines that surplus funds, after payment of debts, will be deposited into the guardians' fund and can be repaid to the debtor upon rehabilitation.³⁰¹

Roestoff is in favour of a further simplification of what is proposed by the Law Reform Commission. She is firstly of the opinion that the period as regards automatic rehabilitation should be shortened and proposes a period of three years – as such a development would be more closely aligned with modern

²⁹⁵ CI 103. See 2014 *Explanatory memorandum* par 103.1.

²⁹⁶ It is an offence where a debtor or his management despite having been expressly asked about his or her or the debtor's financial standing or credit worthiness, falsely conceals his or her or the debtor's insolvent status and as a result thereof obtains credit for more than R500.

²⁹⁷ It is an offence where a debtor or his management at any time within two years before the date of liquidation of his or her estate or the estate of the debtor, with intent to obtain credit or the extension of credit gave false information or concealed any material fact in connection with his or her or the debtor's assets and liabilities to anyone who became his or her or the debtor's creditor.

²⁹⁸ See also 2014 *Explanatory memorandum* par 104.1.

²⁹⁹ The reason for this inclusion is to ease creditors' burden of proof in instances where insolvents have committed offences; 2014 *Explanatory memorandum* par 101.4.

³⁰⁰ 2014 *Explanatory memorandum* para 14.2 and 104.3 and the discussion above.

³⁰¹ See also 2014 *Explanatory memorandum* par 14.2.

trends favouring a fresh start as early as possible.³⁰² She submits that in some instances³⁰³ it should even be possible to approach the court for a further shortening of the period. However, it should be possible for an interested party to apply for the suspension of the automatic rehabilitation and an insolvent who acted fraudulently or who is guilty of any offence in terms of the Act should not be able to obtain an automatic rehabilitation. The same should apply in instances where it is not the first time that the insolvent's estate is liquidated. In such instances the court should retain its discretion to grant the rehabilitation of the insolvent. As regards the effect of rehabilitation, Roestoff proposes that the legislature should state unequivocally that it would extinguish all pre-sequestration debt and that an undertaking to pay such debt thereafter should, in line with the fresh-start principle, not be allowed. In conclusion she proposes that debt resulting from alimony, the intentional assault or killing of another and driving under the influence of alcohol, as well as fines or a person's punishment in accordance with the Insolvency Act should not be extinguished.³⁰⁴

An aspect that, from a debt-relief perspective, has the potential to enhance the outcome of the discharge and therefore the probability of a fresh start is the period in which negative information relating to a debtor's insolvency may be displayed on his credit record. In this regard regulation 17 of the regulations promulgated in terms of the National Credit Act³⁰⁵ provides that credit information relating to sequestration orders may only be displayed and used (for purposes of credit scoring or credit assessment) for a maximum period, from the date the order was granted, of five years or until a rehabilitation order is granted. However, the same period applies as regards information relating to a rehabilitation order, which obviously dilutes the possibility of a true fresh start. This is contrary to international principles and guidelines in that once the discharge has been granted, the debtor should have full access to financial

³⁰² See also the international principles and guidelines that require a discharge not to be in the too distant future; ch 2 par 2.7.

³⁰³ The circumstances that she refers to are set out in cl 101(1)(a) and (b) of the 2015 Insolvency Bill.

³⁰⁴ Roestoff *in Kritiese evaluasie* 395–401. International guidelines accept the exception of alimonies to especially children, but do not recommend exceptions for fines and damages; ch 2 par 2.7.

³⁰⁵ GN R 489 of 31 May 2006.

activities.³⁰⁶ Another procedural attribute that may potentially hinder a true fresh start upon rehabilitation is that, although rehabilitation relieves the insolvent of every disability as a consequence of sequestration, such relief is only automatically available after the substantial period of ten years has lapsed.

3.4 Statutory composition

Section 119 of the Insolvency Act provides for a statutory composition with creditors. However, this procedure does not constitute an alternative to sequestration proceedings as it may only be invoked after the first meeting of creditors in sequestration proceedings has taken place.³⁰⁷ Furthermore, the *World Bank Report* expressed the sentiment that negotiated settlements' benefits are mostly illusory.³⁰⁸

The insolvent must make the offer in writing and through the trustee of the insolvent estate.³⁰⁹ Once the insolvent has disclosed his offer to the trustee, the trustee will decide on the viability thereof. If the trustee finds that creditors will probably accept the offer he will forward a copy thereof, together with his report thereon, to proven creditors.³¹⁰ At the same time, the trustee will give notice of a creditors' meeting where the proposal will be considered.³¹¹ At the meeting, the offer must be accepted by proven creditors representing at least 75% in value and in number. The fact that passive creditors are bound to the settlement is in line with international principles and guidelines.³¹² If the offer is accepted, the composition binds all concurrent creditors³¹³ and the master will certify the composition subject to certain provisos.³¹⁴ These are that either payment in

³⁰⁶ Ch 2 par 2.7.

³⁰⁷ S 119(1). Therefore, the formal process will continue if the proposed composition fails.

³⁰⁸ See ch 2 par 2.6.2.1. The WB generally refers to settlement procedures as informal, even where they are regulated statutorily; *WB Report* 45 *et seq.* Other sources distinguish between formal and informal procedures on the basis of statutory regulation; see Fletcher *The law of insolvency* 45 and Josling 'Alternatives to bankruptcy' 10.47 and 10.48.

³⁰⁹ S 119(1).

³¹⁰ S 119(2). Where the trustee is of the opinion that creditors will not accept the offer of composition, he must inform the insolvent of his opinion and that he does not propose that a copy thereof should be forwarded to creditors. However, the insolvent may in such circumstances lodge an appeal to the master; s 119(3) and (4).

³¹¹ S 119(3).

³¹² Ch 2 par 2.7.

³¹³ S 119(7) and s 120(1).

³¹⁴ S 119(7).

terms of the composition has been made or security for such payment has been posted; that no priority is given to one creditor (above another) to which he would not have been entitled under the ordinary distribution of the estate; and that the agreement is not subject to conditions relating to the insolvent's rehabilitation. Further, where security is provided for, the nature thereof must be fully described.³¹⁵ It is unfortunate that passive creditors are able to hinder acceptance as the procedure does not provide that only the votes of creditors who attended the meeting would be taken into account. This is in contrast with international principles and guidelines.³¹⁶ However, in line with international principles and guidelines, the procedure is backed by formal procedures should it fail (as the formal proceedings will continue).³¹⁷

A composition that includes an undertaking to benefit any person in exchange for an acceptance of the offer of composition is void. A person who has accepted or negotiated such a benefit is liable to pay a fine³¹⁸ to the estate³¹⁹ and is guilty of an offence.³²⁰

The effect of the composition is not only that it binds all concurrent creditors, but also that, if the composition so provides, the insolvent may recover property.³²¹ Furthermore, the insolvent may, with three weeks' notice, immediately apply for his rehabilitation if 50 cents in the rand were paid in respect of proven claims or security has been provided therefor.³²² To render rehabilitation subject to a certain level of payment to creditors runs counter to international principles and guidelines.³²³ The composition does not have an impact on secured or preferent

³¹⁵ *Ibid.*

³¹⁶ Ch 2 par 2.7.

³¹⁷ *Ibid.*

³¹⁸ Equal to the amount of his claim plus the value of the benefit as well as his part in accordance with the composition.

³¹⁹ S 130.

³²⁰ S 141.

³²¹ S 120(2).

³²² S 124(1). See par 3.3.4 as regards rehabilitation in general.

³²³ Ch 2 par 2.7.

creditors, which is in line with international principles and guidelines,³²⁴ creditors of the insolvent's spouse or the insolvent's securities.³²⁵

The trustee must as far as is practical see to it that the composition is fulfilled by, amongst others, making payments to creditors in accordance with the composition.³²⁶

The 2015 Insolvency Bill has retained the statutory composition. It is contained in clause 119 under the title 'post-liquidation composition'.³²⁷ The Law Reform Commission aspires to encourage compositions through amendments to the current procedure as it is of the opinion that compositions, in comparison with formal procedures, offer both debtors and creditors more advantages. It reasons that a debtor's assets are more valuable to him than the amount which they would realise in a forced sale. Further, an extensive period normally lapses before creditors receive a dividend.³²⁸

The most important proposed amendment to the existing procedure is that the required percentage of creditors voting in favour of the composition is set at a mere majority in number and two-thirds in value of *concurrent* creditors who vote on the offer.³²⁹ The fact that the clause refers to those who vote is in line with international principles and guidelines as, as was noted above, passive creditors should not be able to hinder agreements.³³⁰ Also, the 50-cents requirement in relation to the early eligibility for rehabilitation is not repeated in the 2015 Insolvency Bill, which will probably result in more debtors qualifying for an early discharge and accords with international guidelines.³³¹ It is also proposed that a debtor may at any time after a statement of affairs was lodged and after the

³²⁴ *Ibid.*

³²⁵ Ss 120 and 122.

³²⁶ S 123.

³²⁷ See ch 5 par 5.2 for a discussion of the proposed pre-liquidation composition.

³²⁸ 2014 *Explanatory memorandum* par 119.2.

³²⁹ Cl 119(4). According to the Law Reform Commission, the current percentages and the fact that they relate to all proved creditors discourage the acceptance of a composition. The newly proposed percentages are similar to those in the United States of America and in Scotland; 2014 *Explanatory memorandum* par 119.2.

³³⁰ Ch 2 par 2.7.

³³¹ *Ibid.*

issuing of the first liquidation order provide his liquidator with a written offer of composition.³³²

Another important proposed amendment is contained in clause 119(8) and provides as follows:

If the offer of composition contained incorrect information which caused a majority of creditors to vote in favour of its acceptance or if the debtor or another person has failed to give effect to any term of the composition or to comply with this section, the liquidator may, despite the absence of a resolution of creditors authorising him or her to do so, approach the court for the cancellation of a composition, the setting aside of an order providing for the discharge of a first liquidation order or an order setting aside a final liquidation order, or for other relief.³³³

The second proviso to the existing section 119(7), which renders any condition relating to rehabilitation of no effect, is not repeated in the 2015 Insolvency Bill as the commission sees no clear reason why this should be the case.³³⁴ Clause 119(6) also provides that, subject to clause 119(5), a condition that provides for the discharge of a provisional liquidation order or the setting aside of a final order upon acceptance of the offer of composition is valid. However, clause 119(5) renders an offer of composition invalid where it requires a creditor to obtain a benefit (as against another creditor) to which he would not have been entitled if the estate had been liquidated in the ordinary course of the procedure.

3.5 Evaluation in terms of the right to equality

In this paragraph some remarks are made as regards the right to equality, in terms of both the South African Constitution and the Equality Act, in relation to the sequestration procedure and more specifically the advantage for creditors requirement. Both positions are considered as different procedures and remedies are involved and because the Equality Act furthers the South African understanding of the right to equality.³³⁵

³³² CI 119(1). Roestoff *in Kritiese evaluasie* 395 is in favour of all of these proposals.

³³³ This clause was inserted as a lacuna currently exists in that creditors cannot apply for a cancellation of the composition where its terms are breached; see 2014 *Explanatory memorandum* par 119.9 and *Blou v Lampert and Chipkin* 1970 (2) SA 206 (T).

³³⁴ 2014 *Explanatory memorandum* par 119.3.

³³⁵ See ch 1 par 1.1 for the framework against which this paragraph measures the advantage for creditors requirement.

Applying the constitutional test as set out in *Harksen v Lane*³³⁶ to the advantage for creditors requirement, it is safe to say that the requirement at the very least differentiates between categories of people as it distinguishes between those who can prove an advantage for creditors and those who cannot. Although the exclusion of debtors from the procedure *as such* may already constitute unfair discrimination, this aspect is not further discussed in this chapter, as it can only be properly determined once the secondary statutory debt relief measures, discussed in chapter 4,³³⁷ have been considered. However, at this stage it can be said that the advantage requirement differentiates or discriminates (if one accepts that socio-economic status resorts under the listed ground of ‘social origin’) as only those debtors who are allowed access to the sequestration procedure qualify for a discharge of debt. This is because the two secondary statutory procedures do not provide for a discharge.³³⁸

The next step in the enquiry is to establish whether this differentiation is based on a legitimate government purpose. As was discussed above, the main object of the Insolvency Act is to regulate the sequestration process by ensuring an orderly and fair distribution of assets – to the advantage of the creditors of an insolvent estate.³³⁹ It is logical to allow entrance to this procedure only to those debtors who can at least prove some form of advantage in applying this cumbersome and costly procedure³⁴⁰ which will eventually lead to a discharge. In other words, it would not make sense to employ this intricate and costly procedure where its application would be all for nought and therefore its object is legitimate.³⁴¹ Nevertheless, even if the differentiation bears a rational connection to a legitimate government purpose, it may still amount to discrimination. Therefore, the second step in the test is to determine whether the differentiation amounts to unfair discrimination, which was defined in *Prinsloo v Van der Linde* as meaning ‘treating persons differently in a way which impairs their fundamental

³³⁶ 1998 (1) SA 300 (CC).

³³⁷ See para 4.2 and 4.3.

³³⁸ See par 3.1 and ch 1 par 1.1.

³³⁹ See par 3.3.2.2.

³⁴⁰ Roestoff and Coetzee 2012 *SA Merc LJ* 76 and Coetzee and Roestoff 2013 *Int Insolv Rev* 208.

³⁴¹ See s 9(1) of the Constitution.

dignity as human beings, who are inherently equal in dignity'.³⁴² As far as discrimination is concerned, the apparent socio-economic difficulties that riddle those individuals who form part of the lower section of the South African economy, and who form a major part of the excluded group of debtors,³⁴³ are associated attributes and characteristics with the potential to impair the human dignity of the excluded individuals. Therefore, the exclusion of some insolvent natural person debtors from the discharge that the sequestration procedure brings about has the potential to qualify as discrimination as it adds to such individuals' already undignified financial situation by keeping them in a state of perpetual over-indebtedness. The differentiation therefore qualifies as discrimination.

The next question is whether such discrimination constitutes unfair discrimination, which boils down to the impact thereof on the complainant and others in the same situation. In employing the factors to be considered, as was set out in *Harksen v Lane*,³⁴⁴ the probable impact that the discrimination would have in some instances is apparent and links with the reason why in some instances the differentiation amounts to discrimination. This is so as most of those who do not have the option of ridding themselves of excessive debt, as opposed to their more well-to-do fellow citizens who can prove advantage for creditors, generally find themselves in a lower socio-economic position. Although the present argument does not necessarily accept that discrimination takes place on a listed ground, it has been mentioned that it could take place on the grounds of 'race'³⁴⁵ or 'social origin'. If it is found that discrimination takes place on the basis of race specifically, the debtors concerned will be able to argue that they have suffered from patterns of disadvantage in the past.³⁴⁶ The second factor relates to the nature of the provision and its purpose. In this regard it has to be noted that the advantage for creditors requirement was not devised to harm excluded debtors and that it seeks to achieve a worthy purpose, namely, to only allow debtors into the system where the costly sequestration procedure would

³⁴² *Prinsloo v Van der Linde* 1997 (3) SA 1026 (CC).

³⁴³ See in general Coetzee and Roestoff 2013 *Int Insolv Rev* 188.

³⁴⁴ 324.

³⁴⁵ See ch 1 par 1.1.

³⁴⁶ See the first factor as regards unfairness in *Harksen v Lane*.

yield some return for creditors or, in other words, where it would be worthwhile to employ the procedure. However, as far as ‘any other relevant factors’ are concerned,³⁴⁷ the discrimination has, as was already mentioned, the potential to affect the rights and/or interests of excluded debtors severely as they will not be able to find recourse in the form of a discharge in secondary measures. They will therefore potentially be slaves of their undignified financial situation indefinitely. In instances where this is the case, such debtors’ fundamental human dignity will clearly be impaired. Also, such inescapable financial bondage will lead to further socio-economic deprivation. It can therefore be said that the advantage for creditors requirement may have a potentially grave impact on those who are not able to satisfy same on socio-economic grounds.

The final step in the enquiry is to ascertain whether the established unfair discrimination is justifiable in terms of the limitations clause. However, it is presumed that it is not as the clause’s application has never led to any challenged laws being upheld.

Turning to a discussion of the Equality Act, it is notable that socio-economic status was not included in paragraph (a) of the Act’s definition of prohibited grounds, but that the legislature nevertheless regards it as an important ground and has defined the concept in section 1(1) as including

a social and economic condition or perceived condition of a person who is disadvantaged by poverty, low employment status or lack of or low-level educational qualifications.

The exclusion that the advantage for creditors requirement brings about can in many instances be traced back to poverty, low employment status and low levels of education. Further application of the standards of the Equality Act to such instances makes it clear that discrimination takes place as, like in instances where the exclusion is based on socio-economic status, the advantage for creditors requirement directly and indirectly withholds benefits, opportunities and advantages from individuals as they will not be able to receive the eventual discharge that the sequestration procedure brings about. Furthermore and within

³⁴⁷ The third factor as regards unfairness as set out in *Harksen v Lane*.

the present context, socio-economic status at least resorts under paragraph (b) of the definition of prohibited grounds as the human dignity of a large group of excluded individuals is undermined as was illustrated in the constitutional discussion.³⁴⁸ These debtors are also adversely and seriously affected in a manner at least comparable to discrimination on a listed ground. It further perpetuates systemic disadvantage as members of the excluded group are mostly from the lower tiers of the economy and are consequently already in a disadvantaged socio-economic position.

In view of the above, I believe that at least a *prima facie* case of discrimination can be made out and that the burden of proof to establish fairness will therefore shift to the defendant/respondent in terms of section 13. Even though the unfairness of the discrimination will be presumed it must still, in disputed cases, be determined in terms of section 14. In this regard, I refer to only some of the factors set out in subsection (3) as a discussion of others will only be possible once the secondary statutory debt relief measures have been considered in chapter 4.³⁴⁹ The factors to be considered later are whether the discrimination is systemic in nature,³⁵⁰ whether there are less restrictive and disadvantageous means to achieve the purpose,³⁵¹ and whether (and, if so to, what extent) steps have been taken to address the disadvantages or to accommodate diversity.³⁵² As regards the remaining factors, it has already been argued in the context of the Constitution that the exclusivity of the broader insolvency law impairs human dignity.³⁵³ The likely impact on a large percentage of the excluded group³⁵⁴ has also been discussed above. Subsection (3)(c) is important in the present context as it refers to the position of the complainant in society and whether he suffers from patterns of disadvantage or belongs to a group that suffers therefrom. In this regard, some excluded debtors' circumstances make for excellent examples of persons suffering from patterns of disadvantage as they are already left with

³⁴⁸ See also ch 1 par 1.1.

³⁴⁹ Para 4.2 and 4.3.

³⁵⁰ S 14(3)(e).

³⁵¹ S 14(3)(h).

³⁵² S 14(3)(i).

³⁵³ S 14(3)(a).

³⁵⁴ S 14(3)(b).

no income and no assets. Their over-indebtedness only extends their financial woes. Furthermore, if it should be argued and found that the distinctions are indirectly drawn on the basis of race, subsection (3)(c) will be even more pertinent in its application due to South Africa's history of racial discrimination. As regards the nature and extent of the discrimination, it is (as was mentioned) based on socio-economic grounds and results in the financial slavery of a large group of debtors, which can, in some instances, endure indefinitely.³⁵⁵ Nevertheless, the advantage for creditors requirement does strive to achieve a legitimate government purpose.³⁵⁶ However, when the cumulative effect of the factors considered are taken into account it seems that, also in terms of the Equality Act, the advantage for creditors requirement unfairly discriminates against some of those who are excluded. This group is typically formed by the so-called No Income No Asset (NINA) debtors.

3.6 Conclusion

In this chapter, aspects of the Insolvency Act relating to debt relief were considered. This was done to determine the extent to which the Act provides relief and its effectiveness within the present South African socio-economic context. The discussions focused mostly on the sequestration procedure.

In view of the socio-economic environment that South-Africans are faced with today,³⁵⁷ it is clear that the sequestration procedure on its own does not provide sufficient and efficient debt relief. This is so despite the fact that, due to its discharge attribute, the procedure is regarded as the country's primary debt relief measure. The Act's archaic philosophy, namely, that advantage for creditors is in all instances required, and the fact that secondary statutory measures do not lead to a discharge, are impacting on the modern economy³⁵⁸ as well as societal attitudes and behaviour.³⁵⁹

³⁵⁵ S 14(3)(d).

³⁵⁶ S 14(3)(f).

³⁵⁷ See ch 1 par 1.1.

³⁵⁸ *Ibid.*

³⁵⁹ See for instance the discussion of friendly compulsory sequestration applications in para 3.3.2.1 and 3.3.2.2.

Before the provisions of the existing Act were considered the origins of some of the Act's procedures were traced and it was found that some principles were derived from Roman law. Although Roman law was initially penal in nature, it later provided for a debtor's surrender of his estate to prevent execution against his person. This was known as *cessio bonorum*. It is interesting that in Roman law, in contrast with contemporary insolvency law, *cessio bonorum* could be claimed as a right although the procedure did not lead to a discharge of debt.³⁶⁰ However, when *cessio bonorum* became part of Roman-Dutch law it regressed, at least as far as debt relief is concerned, as it was then considered to be a privilege. In this regard little has evolved between then and now as the acceptance of a voluntary surrender application is still regarded as a privilege today. Notable liberal features of early Cape law are that creditors were not able to secure a debtor's sequestration and did not take part in the administration of the estate. In turn, the predecessor of the present Act, the 1916 Insolvency Act, did not contain the advantage for creditors requirement and therefore some courts regarded the sequestration procedure as a true debt relief measure. It can consequently be said that earlier versions of natural person insolvency law were in some respects closely aligned with contemporary international principles and guidelines.³⁶¹

As far as debt relief is concerned, the 1936 Insolvency Act, in comparison with the 1916 Act, has taken some backward steps. This is because the present sequestration procedure is only indirectly regarded as a debt relief measure due to its object of regulating the sequestration process to ensure an orderly and fair distribution of assets to the advantage of creditors.³⁶² In this regard international principles and guidelines warn that it will always be problematic to extract value from natural person insolvents and that the focus of insolvency laws should rather be on debt relief and rehabilitation of debtors – which will benefit not only the debtor but also creditors and society at large.³⁶³ The fact that creditors may apply for compulsory sequestration is also contrary to international guidelines as

³⁶⁰ See the discussion of the *Ford* case in par 3.3.2.2.

³⁶¹ Par 3.2.

³⁶² Par 3.3.1.

³⁶³ Ch 2 par 2.7.

the procedure can be misused. Furthermore in this regard, acts of insolvency are out-dated as the focus should be on the inability to pay and not on 'wrongful' acts by the debtor.³⁶⁴ Nevertheless, not only does the South African system provide for creditor applications, the formal and substantial requirements, most notoriously the advantage for creditors requirement, are applied less strictly in such instances. This in turn has led to further problems in that debtors opted to make use of the compulsory route by enticing friends to apply for their sequestration. Instead of at least recognising (which could have spurred reform) that such endeavours point to larger systemic problems, namely, the need for alternative measures leading to a discharge, courts in some instances view such applications as an abuse of process. In this regard some judgments, contrary to the principle of separation of powers, went so far as to prescribe additional requirements in instances where it was suspected that the application was a friendly one. As, amongst others, voluntary surrender applications are brought on an *ex parte* basis and no collusion is necessary (as the debtor is also the applicant), courts have of late become stricter in this regard. What is worse is that the Law Reform Commission does not appreciate the seriousness of the predicament that natural person insolvents find themselves in as the 2015 Insolvency Bill adds further procedural layers and requirements to voluntary surrender applications. In this regard a provisional order, which will increase costs, and the need to provide security are proposed. A substantial requirement, namely, that the debtor must prove that the debt review procedure in terms of the NCA has been applied or that it would not serve a useful purpose, has also been added. A court will further only allow a provisional order in instances where the post- or pre-liquidation composition procedures or the administration order procedure are not more appropriate. It is submitted that in this regard the onus would also be on the debtor to assure the court as to the reason why such procedures would not suffice – something which debtors are not readily equipped to do. In fact, the most recent international guidelines suggest that a decision as to the most appropriate procedure should best be left to disinterested government institutions.³⁶⁵ The 2015 Insolvency Bill furthermore proposes that

³⁶⁴ *Ibid.*

³⁶⁵ Par 2.7.

compulsory applications be retained and stricter requirements as regards security are also proposed in this regard. The commission is of the opinion that such reforms will ensure that the advantage requirement is complied with and that friendly applications are prevented. It is submitted that the legislature should rather focus its attention on devising proper alternative debt relief measures as this will automatically solve problems of 'abuse'. Even though secondary statutory debt relief procedures are only discussed in the next chapter, the latter statement can be made at this stage as it is already clear that only the sequestration procedure provides for a discharge of debt. Returning to the discussion of compulsory proceedings, the Law Reform Commission has, in line with international best practices, done away with acts of insolvency. However, some remnants thereof are to be found under what is regarded as being 'unable to pay'.³⁶⁶

As regards the meaning of the advantage for creditors requirement, upon which the whole sequestration procedure is built, it is curious that such an important concept has not been defined in the Act. However, case law suggests that it refers to pecuniary benefits or more specifically a non-negligible dividend to be paid to concurrent creditors. Due to this very objective, creditors heavily participate in the procedure and debtors are excluded on financial grounds which are both in contrast with international principles and guidelines.³⁶⁷ However, notwithstanding the above criticism against this pro-creditor procedure, such a cumbersome and costly procedure would be all for naught if it does not turn out some monetary benefit for creditors. Provided that proper alternative statutory debt relief procedures are available, the Law Reform Commission's proposed retention of the requirement is supported as a procedure of such nature is probably necessary in complicated cases where sufficient assets are available to pay for the process and result in a proper dividend for creditors.³⁶⁸ However, when considering the South African socio-economic environment it is obvious that if alternative procedures leading to a discharge existed, the sequestration

³⁶⁶ Para 3.3.2.1 and 3.3.2.2.

³⁶⁷ Ch 2 par 2.7.

³⁶⁸ Par 3.3.2.2.

procedure will only be employed in the absolute minority of cases as debtors would not be pressed to ‘misuse’ its machinery.³⁶⁹

As regards the effect of secondary statutory debt relief measures on voluntary surrender applications, it was established that the interplay between the administration order procedure and the voluntary surrender procedure does not result in any problems. This is because the Magistrates’ Courts Act provides that an administration order is no bar to a sequestration order. On the other hand, the effect of a sequestration order is so far-reaching that it would be both impractical and impossible to obtain an administration order where an estate has already been sequestrated. However, the effect of the NCA’s ‘remedial measures’ on applications for voluntary surrender is not so clear. This can mostly be attributed to the legislature’s failure to address the issue which has led to controversial judgments in this regard – some of which have introduced a new stumbling block in that debtors must satisfy the court that the procedures contained in the NCA would not be more beneficial than the ‘blunter instruments afforded in terms of the voluntary-surrender remedy under the Insolvency Act’.³⁷⁰ Although it was argued that the *Ford* judgment did not technically elevate debt review as an additional requirement in voluntary surrender applications, the 2015 Insolvency Bill sets out to do just that.³⁷¹ It must yet again be emphasised that international guidelines prefer the position where the choice as regards the most suitable procedure is left to disinterested public agencies.³⁷² However, proper alternative procedures leading to a discharge must first be devised. In summary, if the issue of adequate alternative procedures leading to an eventual discharge of debt is duly addressed, many subsidiary issues will also fall away.

When considering the exclusion and/or exemption of property it should be kept in mind that the relevant provisions are directly linked to the debtor’s rehabilitation and the probability of him making a fresh start. In this regard the Insolvency Act is sorely lacking. Even though the Law Reform Commission proposes the

³⁶⁹ See ch 1 par 1.1.

³⁷⁰ *Ex parte Ford* 381.

³⁷¹ Par 3.3.2.3.

³⁷² Ch 2 par 2.7.

extension of such provisions, the proposals are still extremely limited in range and scope. This raises the question whether some of these exemptions mean anything in practice. One example of the short-sightedness of the proposals is that the debtor cannot retain beds where they are not ‘necessary’. The second-hand value of a bed is arguably very low and it is doubtful whether the amount realised will even cover the costs of the sale, not to mention the unlikelihood of increasing dividends to concurrent creditors. If one further accepts, in line with the advantage for creditors requirement and what it entails, that the costly sequestration procedure should only be utilised in instances where substantial value is to be found, the limitation of the categories and especially the values placed on them are absurd. The 2014 *Explanatory memorandum* states that the majority of commentators did not support a proposal that a vehicle, as a primary means of transport, should be excluded from the insolvent estate, one of the dull reasons being that ‘the provision of a vehicle at the cost of the estate is an unjustified luxury’.³⁷³ It seems that the subject did not receive sufficient consideration, notwithstanding the poor public transport system in South Africa and the fact that the loss of a vehicle may also result in the loss of employment. The evident inadequacy of the proposed exemptions, and especially the unwillingness to consider the exclusion of a vehicle, create the impression that the commission is not serious in making available to the debtor rudimentary property that is essential for a basic minimum standard of living as is advocated in the 2014 *Explanatory memorandum*, not to mention a true fresh start.³⁷⁴ International instruments, in contrast, favour a standards-based approach that exempts most property from the estate as a matter of course in jurisdictions where debtors have limited personal assets – such as in South Africa.³⁷⁵ In the unlikely event that all natural person insolvents would in future be able to access the sequestration procedure, such approach would make sense. However, if the broader insolvency system provides for alternative measures, suited to debtors’ specific circumstances that will all eventually lead to a discharge, such an approach may not be beneficial as the sequestration process will only be utilised in instances where there are in fact assets of substantial value. Nevertheless,

³⁷³ See par 14.6.

³⁷⁴ See par 14.4.

³⁷⁵ Ch 2 par 2.7.

even then the narrow range and low levels of exemptions cannot be justified as a balance between maximum creditor returns and the debtor's ability to make a fresh start should be attained. As regards housing, the Law Reform Commission's ignorance of constitutional imperatives in relation to housing and the possible impact thereof on natural person insolvency procedures are unacceptable in a constitutional democracy. It is puzzling that, in light of the developments that have occurred in individual enforcement procedures, the 2014 *Explanatory memorandum* does not even refer to such events. The research by Steyn and her proposals in the context of natural person insolvency law provide a firm basis on which the commission should devise proper policy as regards housing.³⁷⁶

The discharge is the most important aspect relating to the debtor's rehabilitation and therefore international principles and guidelines prescribe that it should be as wide as possible to provide him with the best chance of making a new start.³⁷⁷ In this regard the wide discharge that the Insolvency Act provides is commended. The discharge further relieves the insolvent from every disability relating to his sequestration. However, the fact that adverse information relating to the debtor's rehabilitation may be displayed by credit bureaux for a period of five years puts the debtor's chances of a true fresh start at risk. It is also in contravention with international principles and guidelines.³⁷⁸ Nevertheless, as was indicated, rehabilitation is not a right and is subject to the court's wide discretion.³⁷⁹ The 2015 Insolvency Bill proposes a simplification of aspects relating to rehabilitation. An important proposed amendment is that the six-month period, where no claims have been proved, should be extended to four years. An extension of this term is supported. Another proposal is that the 50-cents limit that allows an insolvent to apply for rehabilitation immediately after a composition has been accepted should be omitted. Such a development is also supported as it would encourage compositions. Nevertheless, it is agreed with Roestoff that the proposed provisions should be simplified even further and that an automatic rehabilitation

³⁷⁶ Par 3.3.3.

³⁷⁷ Ch 2 par 2.7.

³⁷⁸ *Ibid.*

³⁷⁹ See *Ex parte Snooke* 2014 (5) SA 443 (FB).

after a period of three years, as opposed to ten years, is favoured.³⁸⁰ The onus should thus shift to interested parties who will be able to oppose the automatic rehabilitation in instances where they deem it necessary to do so. An automatic rehabilitation should also not take place where an insolvent acted fraudulently, is guilty of an offence in terms of the Act or in instances where it is not the first time that the insolvent's estate is sequestrated.³⁸¹ In this manner, scarce resources could be saved which would benefit all involved. Roestoff's submission in relation to the optimal term after which the automatic rehabilitation is competent is strengthened in that the *World Bank Report* regards periods beyond three years as social irresponsibility.³⁸² This is supported. Her proposals that the legislature should unequivocally state that rehabilitation would extinguish all pre-sequestration debt and that an undertaking to pay such debts thereafter should not be allowed, are also supported.³⁸³

Turning to the statutory composition, it was established that it (theoretically) is a valuable tool at the disposal of debtors who can put forward an attractive offer compared to what would materialise in terms of the sequestration procedure. By making use of this procedure further costs can be minimised, which could yield a better return for creditors, and creditors may receive a dividend much earlier. From the debtor's point of view it may be beneficial in that he can regain some of his assets and in some instances apply for earlier rehabilitation. However, the *World Bank Report* argues that such merits are often illusory.³⁸⁴ Nevertheless, the procedure mostly adheres to international principles and guidelines in that it is backed by formal procedures should it fail, renders passive creditors bound to a settlement and protects secured creditors' interests.³⁸⁵ Unfortunately, passive creditors are at present allowed to hinder such agreements.³⁸⁶ The 2015 Insolvency Bill refines the procedure by proposing the reduction of the percentage of creditors' votes and that, in line with international principles and

³⁸⁰ Roestoff 'n *Kritiese evaluasie* 395.

³⁸¹ *Ibid.*

³⁸² *WB Report* 86.

³⁸³ Roestoff 'n *Kritiese evaluasie* 400 and par 3.3.4.

³⁸⁴ *WB Report* 46.

³⁸⁵ Ch 2 par 2.7.

³⁸⁶ *Ibid.*

guidelines,³⁸⁷ only concurrent creditors who vote will be reckoned into the required majority vote. It is further suggested that the 50-cents requirement should be abandoned. The statutory composition unfortunately does not increase access to relief as it is only available after sequestration.³⁸⁸

In conclusion, it was found that the exclusivity of the sequestration procedure, because it is the only statutory debt relief measure providing for a discharge of debt, is open to a constitutional challenge on the basis of the right to equality. It was established that it is mostly the advantage for creditors requirement that stands in the way of debtors accessing the fresh start that only the sequestration procedure offers. Although the purpose of the vexed requirement is rational, it fails the remainder of the constitutional test and has consequently been found to unfairly discriminate on the basis of debtors' socio-economic status. The same applies as regards the test put forward in the Equality Act. However, it must be emphasised that this is only the case where the differentiation is based on socio-economic grounds and where the debtor will not be able to obtain a discharge by making use of alternative procedures.³⁸⁹ A discussion of secondary statutory debt relief measures follows in chapter 4.

³⁸⁷ *Ibid.*

³⁸⁸ Par 3.4.

³⁸⁹ Par 3.5.

CHAPTER 4: DEBT RELIEF PROCEDURES

SUMMARY

- 4.1 Introduction
 - 4.2 Aspects of the administration order procedure
 - 4.3 Aspects of the debt review procedure
 - 4.4 Evaluation in terms of the right to equality
 - 4.5 Conclusion
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The basic disadvantage ... is wasted cost in terms of time, money and other resources of thinly spread administrative resources. In many cases, although these systems do achieve many of the goals of natural person insolvency for debtors and society, payment plans do not provide a significant financial return to creditors. The experience of many systems casts doubts on the effectiveness of allocating administrative resources to a process that often produces no direct economic returns for creditors. However, even if payment plans are not especially effective from a financial point of view, they do serve important moral and educational purposes.¹

4.1 Introduction

It was established in chapter 3 that the sequestration procedure in terms of the Insolvency Act² does not provide adequate debt relief to natural person insolvents on its own³ and that if the procedure is viewed as such, it will not withstand constitutional scrutiny as it infringes on the right to equality.⁴ However, the requirement responsible that causes the exclusion of most individuals, namely that of advantage for creditors, serves a rational and important government purpose as it would not be economical (in any sense) to employ such a complex and expensive procedure if it will not result in any monetary outputs. That the procedure is necessary is not in dispute, as estates of value can only be fittingly liquidated by means of its well thought-through procedures. However, in order to save the

¹ WB *Report* 137; see also ch 2 par 2.7.

² 24 of 1936.

³ See ch 3 par 3.6.

⁴ See ch 3 par 3.5.

sequestration procedure from unconstitutionality, it is not only imperative, but also urgent to ensure that proper alternative procedures are in place for those individuals who are not able to prove advantage for creditors in order to secure the discharge that the procedure affords. At present, South African law provides for two other statutory debt relief procedures. These are the administration order procedure in terms of section 74 of the Magistrates' Courts Act⁵ and the debt review procedure provided for by section 86 of chapter 4⁶ part D⁷ of the National Credit Act.⁸ The administration order and debt review procedures can be labelled as secondary debt relief measures as they, unlike the sequestration procedure, do not provide for a discharge of pre-procedure debt. In some instances, where the access requirements allow therefor, either or both of the secondary procedures can in theory be utilised as an alternative to the sequestration procedure. However, not all over-indebted or insolvent natural persons qualify for these secondary measures. This is as both procedures are dependent on disposable income as they are (mainly) repayment plans in nature. Therefore, some of the sentiments expressed in the context of the exclusivity of the sequestration procedure also echo in the discussion here, the most notorious being that in South Africa an individual can be 'too broke to go bankrupt'.⁹

This chapter is dedicated to an examination of the two secondary statutory debt relief procedures to determine their adequacy. In this regard both their adequacy within the factual South African context and their adherence to international principles and guidelines are measured. Access requirements are of special importance to determine the extent to which these procedures provide a form of recourse to the general pool of financially over-committed natural person debtors. The general effectiveness of the two procedures is also considered, with emphasis on the extent to which they provide for actual debt relief. General procedural problems and deficiencies are also highlighted.

⁵ 32 of 1944.

⁶ Ch 4 deals with consumer credit policy.

⁷ Pt D is headed 'over-indebtedness and reckless credit'. For a detailed discussion of reckless credit provisions see ch 5 par 5.5.

⁸ 34 of 2005 (hereafter 'the NCA').

⁹ Rochelle 1996 *TSAR* 319. See also ch 1 par 1.1 and ch 3 in general.

In paragraph two the administration order procedure is considered and the process is briefly set out. A general commentary is followed by a discussion of specific aspects and angles. These relate, amongst others, to access requirements and their effect, the influence of the administration order on secured credit, possible abuse and regulation, the effect of sequestration proceedings on the administration order procedure and, most importantly, the nature and degree of relief offered. A comparison is drawn between the administration order procedure and the sequestration procedure to determine the extent to which debtors receive equal treatment. Proposals and initiatives for reform are discussed and the procedure is finally measured against international principles and guidelines.

The debt review procedure is discussed in paragraph three. The discussion commences with an exposition of the application of the NCA as the debt review procedure is only competent if the NCA finds application. An overview of the procedure follows where some general observations are made. Access requirements and exclusions from the procedure are specifically investigated – also in light of recent amendments brought about by the National Credit Amendment Act.¹⁰ Further aspects under consideration are the impact of sequestration proceedings – more specifically compulsory sequestration – and the administration order procedure on the debt review procedure.¹¹ The relief that the procedure offers in instances where consumers do qualify therefor is considered. A comparison is also drawn between debt review and other statutory debt relief procedures. The debt review procedure is finally measured against international principles and guidelines.

Paragraph four concludes the evaluation of South African secondary debt relief measures in light of the right to equality as all statutory debt relief measures will by then have been detailed.¹² Paragraph five concludes the chapter.

¹⁰ 19 of 2014 (hereafter 'Amendment Act').

¹¹ For a discussion of the effect of statutory secondary procedures on the sequestration procedure see ch 3 par 3.3.2.3.

¹² See ch 1 par 1.1 and ch 3 par 3.5.

4.2 Aspects of the administration order procedure

4.2.1 Overview of and general commentary on the process

The administration order procedure was introduced, under English influence,¹³ to the South African legal landscape by section 74 of the Magistrates' Courts Act.¹⁴

Boraine¹⁵ defines the order as

a debt relief measure available to some debtors that find themselves in financial distress, which affords them the opportunity to obtain a statutory rescheduling of debt sanctioned by a court order.

The administration order involves a relatively simple and inexpensive procedure whereby overcommitted debtors' obligations are rescheduled by the magistrates' courts.¹⁶ These orders are intended for smaller estates where the sequestration procedure would exhaust the estate¹⁷ and the aim is mainly to protect the debtor during a period of financial embarrassment without the need for sequestration.¹⁸ The Supreme Court of Appeal in *Bafana Finance Mabopane v Makwakwa* summarised the main purposes of the administration order procedure in the following terms:¹⁹

[T]o protect debtors with small estates, 'usually ... those who are poor and either illiterate or uninformed about the law or both'.²⁰ It has a second, but also important purpose, which is to ensure that creditors to whom money is owed and due for payment by the debtor are able to recover as much as the

¹³ See Boraine 2003 *De Jure* 219 and Roestoff 'n *Kritiese evaluasie* 406.

¹⁴ See in general Van Loggerenberg *Jones and Buckle* 489–547; Paterson *Eckard's principles* 318–344 and Boraine *et al* 2012 *De Jure* 83–93 for detailed discussions of the administration order procedure.

¹⁵ Boraine 2003 *De Jure* 217–218. In *Bafana Finance Mabopane v Makwakwa* 2006 (4) SA 581 (SCA) 583 the Supreme Court of Appeal confirmed that the administration order procedure is a debt relief measure.

¹⁶ See s 74C. The magistrates' courts are heavily involved in the procedure as will be seen below. International guidelines note that although courts will always have a role to fulfil in natural person insolvency law, their involvement should be the exception and must be specialised. Remaining functions should ideally be counterbalanced by public administrative bodies. However, in developing countries, existing institutional infrastructure should be expanded and procedures simplified rather than developing novel infrastructure; ch 2 par 2.7.

¹⁷ *Fortuin v Various Creditors* 2004 (2) SA 570 (C) 573; *Ex parte August* 2004 (3) SA 268 (W) 271.

¹⁸ *Cape Town Municipality v Dunne* 1964 (1) SA 741 (C) 744; *Fortuin v Various Creditors* 573; *Ex parte August* 271 and *African Bank Ltd v Jacobs* 2006 (3) SA 364 (C) 365. However, as will be seen below, the sequestration procedure is not readily available to natural person debtors who are eligible for the administration order procedure.

¹⁹ 587–588.

²⁰ In this regard the court quoted from *Coetzee v Government of the Republic of South Africa; Matiso v Commanding Officer, Port Elizabeth Prison* 1995 (4) SA 631 (CC) 641 regarding s 65A–65M of the Magistrates' Courts Act. However, the court found it to be of equal importance to administration orders.

administrator permits. There can be no doubt, therefore, that section 74 was enacted in the public interest.²¹

In *Madari v Cassim*²² Caney J accurately described the nature of these orders:

Administration orders under sec. 74 of the Magistrates' Courts Act have been described, I think correctly, by the learned authors of Jones and Buckle on the *Civil Practice of the Magistrates' Courts*, as a 'modified form of insolvency'.²³ This is designed, it seems to me, as a means of obtaining a *concursum creditorum* easily, quickly and inexpensively,²⁴ and is particularly appropriate for dealing with the affairs of debtors who have little assets and income and genuinely wish to cope with financial misfortune which has overtaken them. Creditors have certain advantages under such an order, including the appointment of an independent administrator and the opportunity of examining the debtor. They are not debarred from sequestrating the debtor if the occasion to do so arises.

The administration procedure may thus be seen as a form of insolvency²⁵ or even as an alternative to sequestration under certain circumstances.²⁶ It generally takes the form of a repayment plan. However, in some instances the court may authorise the administrator, appointed by the court and tasked with the administration of these estates, to sell some of the assets in order to distribute the proceeds amongst creditors.²⁷ It can thus be said that the administration order is a hybrid debt relief

²¹ The fact that the procedure takes the interests of the debtor, creditors and the public into account is in line with international foundations of sound insolvency practices; see ch 2 par 2.7.

²² 1950 (2) SA 35 (D) 38.

²³ See Van Loggerenberg *Jones and Buckle* 489–490. That administration orders can be viewed as a modified form of insolvency was approved by the Supreme Court of Appeal in *Weiner NO v Broekhuysen* 2003 (4) SA 301 (SCA) 305. See also *Bafana Finance Mabopane v Makwakwa* 586.

²⁴ See also *Fortuin v Various Creditors* 574 and *Ex parte August* 272.

²⁵ Joubert disagrees with this statement and states that it would be confusing and misleading to say that the administration order procedure is a form of insolvency as the legal consequences of the two procedures (sequestration and administration) are very different in nature; Joubert 1956 *THRHR* 138. Even though the administration order procedure does not provide a discharge of debt and differs from the sequestration procedure in many other respects it can indeed be seen as a debt relief measure as it assists a debtor during a time of financial distress. It can therefore be categorised as part of insolvency law in the wide sense of the word. See also Roestoff 2000 *De Jure* 130.

²⁶ See *African Bank Ltd v Weiner* 2005 (4) SA 363 (SCA) 366.

²⁷ S 74C(1)(b). The fact that assets are not as a matter of course susceptible to realisation and distribution is in accordance with international principles and guidelines, not least as assets are usually more valuable to the debtor than what their economic value represents; ch 2 par 2.7. Furthermore, in South Africa, the majority of debtors making use of the administration order procedure have limited personal assets. Assets that are the subject of a credit agreement as regulated by the NCA may not be realised without the written permission of the seller. See also s 74K(2). This proviso was introduced by s 172(2) and sch 2 of the NCA. It is submitted that the word 'seller' should have been replaced with 'credit provider' as has been done with the

Footnote continues on next page

measure as it makes provision for both the rescheduling of debt and the realisation of assets to service debts.²⁸

A condition precedent for access to the administration order procedure is that a debtor must not have been subject to an administration order that was rescinded within the preceding six months due to the debtor's non-compliance, unless the debtor can prove that the non-compliance with the order was not wilful.²⁹ Another condition is that the total amount of all *debts due* should not exceed the amount determined by the minister by notice in the *Gazette*³⁰ – which is currently set at R50 000.³¹ In *Cape Town Municipality v Dunne* it was held that the term 'debts' means debts 'due and payable' and that it does not include *in futuro* debts.³²

Administration orders are intended to be utilised where the debtor is unable to satisfy a judgment debt or to meet his financial obligations and where he does not have

amendment of s 74K. It seems that this is a mere oversight by the legislature. See par 4.3.1 as regards the scope of application of the NCA.

²⁸ See Boraine *et al* 2012 *De Jure* 87.

²⁹ S 74B(5).

³⁰ S 74(1)(b). In *Da Mata v FirstRand Bank* 2002 (6) SA 506 (W) 511 it was held that where a judgment debt is to be paid in instalments, each instalment should not exceed the total limit as it cannot be said that such instalments are due before the debtor is obliged to pay it. However, in *Jacobs v African Bank* 2006 (5) SA 21 (T) 24, 25 and 29 it was held that the total amount of the judgment debt should be taken into account.

³¹ GN R217 in GG 37477 of 27 March 2014. It is curious that the amount was not revised in 2014 when the government notice that first set the R50 000 limit, namely R1411 in GG 19435, was withdrawn. The R50 000 threshold was merely confirmed.

³² At 745–746. See Greig 2000 *SALJ* 622 for a discussion of *in futuro* debts and criticism on the exclusion thereof. Greig (625) suggests that

the success of an administration order is put seriously at risk where the order cannot include reduction of *in futuro* instalments. Very often the reason for the debtor's parlous financial position is not 'debts the whole amount of which is owing', but in fact a large and unmanageable number of deductions from the debtor's wages or salary as a result of instalment payments on a series of imprudent loan applications.

He further highlights the dubious consequences that in some instances may arise (626) in that if *in futuro* payments are excluded from the purview of administration orders, it often simply becomes a matter of the debtor defaulting on an instalment in order to make the debt one of which the 'whole amount is owing', as nearly all micro-loan agreements have acceleration clauses. The rather bizarre result of this approach is that the moment a debtor is in default of paying an instalment payment he can then apply for the inclusion of the relevant debt in the administration order. However, if instalment payments are up to date, the magistrate is not in a position to reduce payments of *in futuro* debts.

Boraine 2003 *De Jure* 234 and 249 and authorities cited there suggest that the basis of *in futuro* debts should be amended in a new dispensation as it gives rise to many practical difficulties. According to him there is no sound basis for the exclusion. He suggests that the traditional difference between secured and unsecured debts should rather be used to determine which debts should be included and excluded from the procedure.

sufficient assets to attach in satisfaction of such judgment or obligations.³³ If it appears that a debtor, who is before a court for an investigation of his financial circumstances in terms of section 65, also has other debts, the court shall consider whether all the debtor's debts should be treated collectively. If this is the case, the court may postpone the hearing with a view to granting an administration order.³⁴ A court can thus force an administration order on a judgment debtor for his own good.³⁵ However, generally the process of obtaining an administration order entails an application to a magistrate's court in the prescribed format³⁶ coupled with a full statement of affairs³⁷ whereby the debtor seeks an order providing for the administration of his estate and payment of debts in instalments or otherwise.³⁸ The application is lodged with the clerk of the court, and a copy is delivered to each creditor at least three days prior to the hearing.³⁹ At the hearing, creditors may prove their claims⁴⁰ and the debtor may be interrogated.⁴¹ The court considers the circumstances and may then grant an administration order⁴² whereby the estate is placed under administration, an administrator is appointed⁴³ and an amount that the debtor is obliged to pay to the administrator is set.⁴⁴ The latter amount should,

³³ S 74(1)(a). The insolvency test applied in the administration order procedure includes the liquidity test which is in line with international best practice; ch 2 par 2.7.

³⁴ Ss 65I and 74(1).

³⁵ S 65I(2) and (3). See also *Bafana Finance Mabopane v Makwakwa* 586.

³⁶ S 74A(1). Practitioners complain that the procedure is not applied consistently in different courts. The complaints vary from lack of uniformity to lack of capacity. Boraine suggests that the strengthening of debtors' courts acting as specialist courts regarding debt issues will provide a solution. In the alternative, rendering the procedure subject to the supervision of a special official or a special division of the clerk of the court is proposed; Boraine 2003 *De Jure* 232.

³⁷ S 74A(1) read together with s 74A(2). Van Loggerenberg *Jones and Buckle* 496–497 is of the view that although the administration procedure is primarily designed for the protection of the debtor, it is not a soft option and that the court should also protect creditors. In order for the court to exercise its discretion properly it is of importance that all particulars required in the statement of affairs are supplied and that such information is accurate.

³⁸ S 74A(1).

³⁹ S 74A(5).

⁴⁰ S 74B(1)(a)–(d). Where a claim is disputed the court can investigate the matter and allow or reject the debt or part thereof; s 74(B)(2)–(4).

⁴¹ S 74B(1)(e). Creditor participation should preferably be excluded as a matter of course in any insolvency proceedings, except where the estate represents significant value – which is generally not the case in instances where debtors qualify for the administration order procedure; ch 2 par 2.7.

⁴² In accordance with s 74C.

⁴³ See s 74E regarding the appointment of an administrator. Administrators do not resort under a regulatory body and complaints of abuse are rife; see Boraine 2003 *De Jure* 217.

⁴⁴ S 74C(1)(a). See also s 74I. The amount of the periodical payments are determined by the court in accordance with s 74C(2). If the debtor fails to make payments to the administrator as determined in the order, the provisions of s 65A to 65L shall *mutatis mutandis* apply; s 74I(2).

amongst others, take into account the necessary living expenses of the debtor and his dependants,⁴⁵ existing maintenance orders⁴⁶ and, where reasonable, periodical payments in terms of a mortgage bond.⁴⁷ An emoluments attachment order⁴⁸ or a garnishee order⁴⁹ can also be made. It is important to note that the magistrate has a discretion to grant the application, which discretion must be exercised judicially and on proper grounds.⁵⁰ The administration order places minimal limitations on a person's contractual capacity,⁵¹ although he must disclose the fact that he is under administration when incurring a debt.⁵² Prescription is interrupted on the date that the statement is lodged⁵³ and once the order is in force generally no creditor can commence enforcement proceedings for outstanding debt.⁵⁴ Any such proceeding already instituted will be suspended by the administration order.⁵⁵ However, there are exclusions from this moratorium, the most important being a debt in terms of a mortgage bond.⁵⁶ After his appointment, the administrator must as soon as possible draw up a list of creditors setting out the amounts owing to each of them on the day the order was granted.⁵⁷ A person who became a creditor after the order has been granted, may lodge his claim in writing with the administrator who will inform the debtor. However, a dividend will only be paid in respect of such debts where all other

⁴⁵ No standard as regards living expenses has been prescribed for the administration order procedure although the appropriate level of sacrifice, in exchange for relief, is inherently political. A standard needs to be developed and must be supplemented by non-standard allowances such as costs relating to housing, transport and childcare; ch 2 par 2.7.

⁴⁶ The exclusion of alimony is in line with international guidelines; ch 2 par 2.7.

⁴⁷ This feature is in line with internationally accepted principles; ch 2 par 2.7.

⁴⁸ An emoluments attachment order is an order to attach future owing or accruing emoluments from the debtor's employer; s 74D read together with s 65J. See also s 74I(3).

⁴⁹ A garnishee order is an order to attach debt at present or in future owing or accruing to the debtor by another; s 74D read with s 72. See also s 74I(3).

⁵⁰ *Fortuin v Various Creditors* 573; *Ex parte August* 271.

⁵¹ See also Joubert 1956 *THRHR* 139 and 141.

⁵² S 74S. Failure to do so constitutes an offence. However, it does not render the agreement void. S 89(2)(a)(ii) of the NCA renders a credit agreement unlawful if at the time that the agreement was made the consumer was subject to an administration order, the administrator did not consent thereto and the credit provider knew or could have reasonably determined that that was the case.

⁵³ S 74V. Where a debt is not mentioned therein, prescription is interrupted on the date on which the claim is lodged with the court or the administrator.

⁵⁴ S 74P(1). International best practice prefers that a moratorium on debt enforcement should take effect once a case has been filed; ch 2 par 2.7.

⁵⁵ S 74P(2).

⁵⁶ S 74P. The others are a debt that is rejected in accordance with s 74B(3) or where the court has granted leave, subject to conditions that it may impose.

⁵⁷ S 74G(1). A creditor may object to any debt included in the list; s 74(G)(10)(b). A creditor may still prove a claim that was owed before the order was made where it does not appear on the list; s 74G(2)–(6).

creditors have been paid in full.⁵⁸ The principal task of the administrator is to collect payments in terms of the order and distribute them proportionately amongst creditors at least every three months.⁵⁹ The administrator must, when instructed by creditors,⁶⁰ apply for the rescission of the order. This may only happen where the debtor has been in default for fourteen days despite a letter of demand being delivered to him by the administrator and where steps to obtain an emoluments attachment or garnishee order cannot be applied for or have been taken unsuccessfully. Creditors may also instruct the administrator to apply for rescission where the debtor has disappeared.⁶¹ As mentioned, a court may in certain circumstances authorise the realisation of an asset of the estate. This is done through the administrator or, where permissible, by the creditor himself.⁶² If the debtor pays a debt that was due at the time of the order, after the order was granted, the payment shall be invalid. In such circumstances, the administrator may recover the amount from the creditor, unless the latter can prove that he was not aware of the administration order. Where the creditor requested the payment whilst he had knowledge of the administration order, he shall forfeit his claim against the estate.⁶³

The court under whose supervision the order is being executed may on application by the debtor or an interested party re-open the proceedings and call upon the debtor to appear for such further examination as the court may deem necessary. The court may on good cause shown suspend,⁶⁴ amend⁶⁵ or rescind the administration order.⁶⁶ An administration order may at any time, on the written request by the administrator and with written consent of the debtor, be amended by the court.⁶⁷ Where, during an application for rescission of an administration order, it appears to the court that the debtor is unable to pay any instalment, it may suspend the order

⁵⁸ S 74H.

⁵⁹ S 74J(1). S 74O provides that, unless otherwise ordered by the court, the costs in relation to the application of the administration order shall be recovered from the administrator as a first claim against moneys collected by him.

⁶⁰ The majority of creditors must instruct him to do so or must fail to respond.

⁶¹ S 74J(8)–(10). The creditors may also instruct the administrator to institute legal proceedings against the debtor for contempt of court or to take the necessary steps to trace a debtor who has disappeared.

⁶² 74G(8).

⁶³ S 74J(14).

⁶⁴ With or without conditions.

⁶⁵ This is in line with international guidelines that are in favour of plan modification; ch 2 par 2.6.2.5.

⁶⁶ S 74Q(1).

⁶⁷ S 74Q(2).

for a period and on conditions it may deem fit or it may amend the instalments to be paid.⁶⁸ Once the costs of administration and listed creditors have been paid in full, the administrator lodges a certificate at the clerk of the court, whereupon the order lapses.⁶⁹

4.2.2 Access requirements and the effect thereof

From the above it is clear that not all debtors in financial distress are able to apply for an administration order. A debtor who cannot show an advantage to creditors will not only be excluded from the sequestration procedure⁷⁰ but also from employing the administration order procedure where his total debt amounts to more than the stated threshold – which clearly did not keep track of reality.⁷¹ However, it is accepted that a major increase in the threshold may necessitate the introduction of more detailed procedures relating to interrogations, unexecuted transactions and voidable dispositions as the matters that are subject to the procedure will inevitably become more complex.⁷² Another disadvantage relating to access is the exclusion of *in futuro* instalments,⁷³ which prohibits a holistic approach towards solving the debtor's financial problems.

Not only debtors with debt in excess of the threshold are excluded from utilising the administration order procedure as a debt relief measure, but also those with no income and no assets (the so-called NINA debtors). This is so as the procedure is by

⁶⁸ S 74Q(3)(b).

⁶⁹ S 74U. A significant period may pass before such certificate may be issued and in some instances a debtor may be subject to the procedure indefinitely; see also Boraine *et al* 2012 *De Jure* 2012. Generally realistic plans and a period of between three and five years is preferred; ch 2 par 2.7. Roestoff suggests a minimum period of three years; *'n Kritiese evaluasie* 440.

⁷⁰ See ch 3 par 3.3.2.2.

⁷¹ Roestoff proposes that no monetary limit as regards debt should be set as an entry requirement. Creditors' interests would still be protected as the implementation of the sequestration procedure is not excluded by the administration order procedure. Creditors may thus apply for the former in instances where it would result in a better return; 2000 *De Jure* 133 and *'n Kritiese evaluasie* 440–441.

⁷² See Boraine 2003 *De Jure* 233 and 248. Boraine is further of the view that a dramatic increase in the threshold would render the inclusion of the administration order procedure in the Insolvency Act more practical. This is so since the existing procedures contained in the Insolvency Act can then be utilised where more complex issues arise. It is submitted that the implementation of this suggestion will also assist in streamlining the different insolvency procedures. See Roestoff 2000 *De Jure* 129–130 and *'n Kritiese evaluasie* 442–443 where she lobbies for the inclusion of the administration order procedure in the Unified Insolvency Act. The latest version of the Insolvency Bill is the '2015 Insolvency Bill' that is on file with the author.

⁷³ S 74(1)(b).

nature a ‘repayment plan’ and NINA debtors do not have any means from which the administrator will be able to make distributions to creditors.⁷⁴ However, even though the magistrates’ courts are creatures of statute, it may be worthwhile to argue that a magistrate may use his discretion, as provided for to some extent in the section 74, to allow a NINA debtor access to the procedure. If it is found to be possible to allow access to such debtors under certain circumstances, a magistrate can customise the order to fit these unique needs by ordering zero payment plans – which is not a strange phenomenon globally as the majority of natural person insolvency cases represent such plans.⁷⁵ Although a long shot, the idea stems from the wording of section 74(1) which provides that

such court ... may, upon application by the debtor or under section 651, *subject to such conditions as the court may deem fit* with regard to security, preservation or disposal of assets, realization of movables subject to hypothec ... *or otherwise*, make an order ... providing for the administration of his estate and for the payment of his debts in instalments or otherwise [my emphasis].

However, as the word ‘and’ is used it was probably the intention of the legislature that the two possible orders, namely, the administration order and an accompanying order to pay debts in instalments (or otherwise), should always be granted in tandem, although the word ‘may’ can be interpreted to allow a discretion in this regard. It is suggested that the legislature can increase access by inserting the phrase ‘when the debtor’s financial circumstances allow therefor’ after the word ‘and’. Nonetheless, if NINA debtors are allowed access to the existing procedure, they will in all probability remain subject thereto indefinitely as a section 74U certificate may only be issued once all debt subject to the order has been paid in full.

4.2.3 Secured credit

The administration order procedure does not specifically distinguish between secured and unsecured credit. However, secured creditors’ substantive rights are, in line with international principles and guidelines,⁷⁶ protected to some extent in various ways. For instance, claims that would have enjoyed preference in insolvency law

⁷⁴ See in general Coetzee and Roestoff 2013 *Int Insolv Rev* 188 as regards South African NINA debtors.

⁷⁵ See ch 2 par 2.6.2.5.

⁷⁶ Ch 2 par 2.7.

should be paid out in the same order.⁷⁷ Another factor that provides limited protection to secured creditors under certain circumstances is that secured credit is by definition payable in future, and *in futuro* debts are excluded from the operation of the administration order procedure.⁷⁸ In this regard the administration order procedure, in various subsections, regulates the treatment of such debts. The Act for instance allows the court, when determining the amount that the debtor must periodically pay to his administrator, to take cognisance of secured credit by allowing for periodical payments that the debtor is obliged to make under a credit agreement⁷⁹ and a mortgage bond.⁸⁰ It further allows for preference of periodical payments under any other written agreement for the purchase of any assets where the liabilities are payable in instalments.⁸¹ However, the court has a discretion⁸² in allowing preference to such instalments. A proviso to the subsection regulating the possible preference of instalments under the NCA states that the court may refuse to take the periodical payments of the purchase of goods into account if they are not exempt from execution⁸³ or where they are not regarded by the court as household requirements – unless the court decides that in the circumstances it is still desirable to safeguard the goods.⁸⁴ Similarly, in considering the allowance of periodical payments relating to a mortgage bond or other written agreement for the purchase of an asset, the court should take cognisance of all the circumstances in determining

⁷⁷ S 74J(3).

⁷⁸ This will only be the case as long as the debtor has not defaulted on an agreement where an acceleration clause would become effective, which will render the whole amount due and payable thereby rendering the debt subject to the administration order procedure; see the discussion below.

⁷⁹ S 74C(2)(b) refers to credit agreements as defined in s 1 of the NCA (see par 4.3.1). See also s 74A(2)(g). See further *Carltonville Huishoudelike Voorsieners (Edms) Bpk v Van Vuuren* 301.

⁸⁰ S 74C(2)(d). It is submitted that a mortgage bond is in any event included in the reference to credit agreements under the NCA as referred to in s 74C(2)(b). See also s 74A(2)(h) and (i). It should be kept in mind that the moratorium on debt enforcement does not apply to a mortgage bond; s 74P. It seems that the legislature realised both the value of immovable property to the debtor and the special importance of protecting the rights of creditors in this regard. Even though these provisions may at first seem conflicting, it is submitted that they create a balance and allow the court to apply its discretion depending on the individual circumstances at hand. The provisions relating to mortgage bonds are in line with international principles and guidelines as a balance between different interests are attained while mortgage property (which will more often than not represent homes) receives special attention; ch 2 par 2.7.

⁸¹ S 74C(2)(d).

⁸² See *Carltonville Huishoudelike Voorsieners v Van Vuuren* 301 where it was stated that the general principles that a magistrate will take into account is whether the goods are luxury items that the debtor cannot afford, how much has already been paid and whether they are a source of income for the debtor.

⁸³ In terms of s 67. See the discussion of the section in ch 3 par 3.3.3.

⁸⁴ Proviso to s 74C(2)(b).

the reasonableness of the payments and specifically the debtor's income, sums due by him to other creditors and whether it is desirable to safeguard such property.⁸⁵

It is submitted that the administration order procedure does not only have the ability to protect mortgagees, but could, by the same token, come to the assistance of a debtor in securing his home. However, most individuals making use of the administration order procedure are, due to its monetary threshold, from the lower ranks of the economy and do not regularly own a home. It is therefore submitted that the potential protection of the provisions relating to mortgage bonds will only be unlocked if and when the monetary threshold is increased.

Another issue relating to secured debt is that where an acceleration clause in a credit agreement⁸⁶ (where assets formed the object of such an agreement) was triggered and the seller advises the administrator in writing that he elects to demand immediate payment of the sum of the purchase price still owing, such agreement creates a hypothec over the goods in favour of the seller – thereby securing the agreement.⁸⁷ In such instances, the administration order procedure empowers the court to authorise the seller to take possession of the goods and to sell it by public auction.⁸⁸ Where the net proceeds are insufficient to pay the debt in full, the balance may be lodged as a claim with the administrator and the creditor will be entitled to share in the *pro rata* distribution of funds.⁸⁹

⁸⁵ Proviso to s 74C(2)(d). See also *Mnisi v Magistrate, Middelburg* [2004] 3 All SA 734 (T) 743. It is difficult to think of an agreement where s 74C(2)(b) and (d) would not overlap as a mortgage bond and a written agreement for the purchase of an asset where liabilities are payable in future and where the debtor is a natural person will both qualify as a credit agreement in terms of the NCA, more specifically, a mortgage agreement and a credit transaction respectively; see par 4.3.1. Van Loggerenberg *Jones and Buckle* 503 submit that the court may find it desirable to safeguard mortgaged property in view of the amount that has been paid off or the fact that the property is occupied by the debtor and dependants and that the cost of alternative accommodation would not amount to substantially less than the periodical instalments of the agreement.

⁸⁶ As defined in s 1 of the NCA.

⁸⁷ S 74G(7). It further provides that any term or condition in the agreement allowing the seller to dissolve or terminate the agreement or to claim return of the goods shall not be enforceable any longer. Where there is no acceleration clause, the seller may cancel the agreement and claim the return of goods since cancellation is not a claim for 'collecting money owing' as provided for by s 74P; see Van Loggerenberg *Jones and Buckle* 513.

⁸⁸ S 74G(8).

⁸⁹ S 74G(9). This structure can be compared with s 84 of the Insolvency Act.

4.2.4 Possible abuse and regulation of the procedure

The administration order procedure is stigmatised and criticised, one of the major reasons for the negativity being the abuse thereof.⁹⁰ Borraine quotes from a media release by the banking council⁹¹ where the financial sector criticises administrations as representing ‘a lucrative, specialised business pursued by certain commercial entities for maximum financial gain’.⁹² Although much of the criticism against the administration order ‘industry’ is justified, I cannot help but comment on this ludicrous statement coming from the proverbial black pot. It is submitted that there is nothing wrong with the private sector taking advantage of business opportunities (for maximum gain – after all, that is the very nature of business). In fact, it is needed where the state does not provide for such services. Specialisation is also to be welcomed. A problem only arises where these business ventures are conducted in a manner that infringes on the rights of debtors and creditors.

As regards the role and function of administrators the Supreme Court of Appeal⁹³ confirmed that it is akin to that of the trustee in sequestration proceedings. This entails that he occupies a position of trust in the collection and distribution of payments in relation to both the debtor and his creditors. He must accordingly carry out his duties independently and impartially in the interests of both parties. It was also confirmed that the administrator occupies a fiduciary position in relation to money collected and that, like a trustee of a sequestrated estate, should take prompt steps to empower creditors to obtain as large a payment of their debts as possible.

The Magistrates’ Courts Act lists some administrative duties of an administrator and empowers the court to deal with non-compliance thereof.⁹⁴ However, it is submitted that due to the already dire financial situation in which the debtor finds himself, he is probably not in a position to acquire legal (or other) assistance to firstly investigate

⁹⁰ See in general Borraine 2003 *De Jure* 217 and specifically 24 and 230–232. See *idem* 233–234 regarding the position of administrators in particular. See further Borraine and Roestoff 2014 *THRHR* 353; *African Bank Ltd v Weiner* (SCA) and *Stander v Erasmus* 2011 (2) SA 320 (GNP) 324.

⁹¹ Dated 19 June 2002.

⁹² Borraine 2003 *De Jure* 223–224.

⁹³ *African Bank Ltd v Weiner* (SCA) 368 where the court referred with approval to the judgment in the court *a quo* in *African Bank Ltd v Weiner* 2004 (6) SA 570 (C) 575–576.

⁹⁴ S 74J read with ss 74E(2) and 74N. See for instance *African Bank v Jacobs*.

whether the administrator is doing a proper job, and secondly, to hold the administrator accountable, through court procedures, where it is found that it is not the case. In addition, due to the relatively small estates involved it is not worthwhile for credit providers to police and intervene in individual cases in all instances. Unfortunately, beyond the provisions in the Act, that are only as good as they can practically be enforced, administrators are not regulated and are therefore not regularly held accountable for malpractice.

Although this paragraph is not intended to set out in detail all the possible abuses of the procedure, one of the most pertinent abuses deserves special mention and relates to the fees that administrators may charge. In terms of section 74L an administrator may deduct his necessary expenses and remuneration in accordance with the tariff prescribed in the rules before making a distribution to creditors.⁹⁵ However, the section provides that the expenses and remuneration must not exceed 12.5% of the amount collected and are subject to taxation.⁹⁶ Even though the Supreme Court of Appeal in *Weiner v Broekhuysen*⁹⁷ clearly ruled that the fees, expenses or remuneration that an administrator may charge is capped at 12.5% of moneys collected, some administrators persisted in charging excessive fees whilst raising dubious arguments in order to circumvent this judgment.⁹⁸ The matter was finally laid to rest when the Supreme Court of Appeal in *African Bank Ltd v Weiner* held that⁹⁹

it would be unconscionable, on any basis, if the 10% collection fee in Part I of Table B for s 65 proceedings were drawn in addition to the 10% collection fee permitted in Part III for s 74 administrations. There is only one operative collection, and that is the collection under s 74, for which the collection fee of 10% is specified as part of the 12.5% maximum permitted in s 74L(2). If a further collection is alleged to take place by virtue of s 65, no additional fee can be collected in respect of it as a 'cost' under s 74L.

⁹⁵ S 74L(1)(a). A portion of money collected may also be retained to cover the costs that the administrator may have to incur if the debtor defaults or disappears; S 74L(1)(b). See *African Bank Ltd v Melvyn Weiner* (SCA) 369 *et seq.*

⁹⁶ S 74L(2).

⁹⁷ (SCA) 314. See also *African Bank Ltd v Melvyn Weiner* (SCA) regarding fees and costs in general.

⁹⁸ See for instance the arguments of Webbstock in 2002 August *De Rebus* 59.

⁹⁹ 373. Mr Webbstock appeared in person to further his arguments.

4.2.5 Effect of sequestration proceedings on the administration order procedure

An administration order is no bar to the sequestration of a debtor's estate¹⁰⁰ and an application for an administration order may constitute an act of insolvency.¹⁰¹ There are two schools of thought relating to the considerations that should apply where an application for the sequestration of an estate of a debtor under administration is lodged. On the one hand, it was held in *Madari v Cassim*¹⁰² that where a debtor has lodged an application for an administration order and a court thereafter has to decide whether to grant a sequestration order, the position of creditors under an administration order versus the position under sequestration has to be considered. In *Trust Wholesalers v Woollens (Pty) Ltd v Mackan*¹⁰³ the court came to an opposite conclusion and held that the 'methods of dealing with the debtor's affairs' should not be compared. Therefore, according to this line of thought, the proposed sequestration should be considered in a vacuum. Van Loggerenberg prefers the former approach:¹⁰⁴

In comparing the situation of creditors under an administration order and their situation if there is a sequestration the court will take into consideration the fact that an administration order is eminently suited to deal with the estates of small debtors who have little income and assets, while sequestration is more suitable in the case of elaborate estates where the transactions of the debtor might have been complex and where there is reason to believe in all the circumstances that, after the costs of sequestration are paid, it will result in a payment in respect of the claims of the creditors as a body which is not negligible.

It is doubtful whether the conflicting opinions are generally of major practical concern as an attempt to prove advantage for creditors where estates suited to the administration order are under consideration would, 'more often than not, be elusive'.¹⁰⁵ Nevertheless, the approach of *Madari v Cassim* is preferred.

¹⁰⁰ S 74R.

¹⁰¹ In terms of s 8(g) of the Insolvency Act. See *Madari v Cassim* 38; *Fortuin v Various Creditors* 573 and *Ex Parte August* 271. See ch 3 par 3.3.2.1. Although the procedural aspects relating to the interplay between the two procedures are clearly set out, it creates other uncertainties as a disinterested party does not determine the best suited remedy – which will ensure certainty as regards the route to be taken in future; ch 2 par 2.7.

¹⁰² 38.

¹⁰³ 1954 (2) SA 109 (N) 112.

¹⁰⁴ Van Loggerenberg *Jones and Buckle* 537.

¹⁰⁵ See *Bafana Finance Mabopane v Makwakwa* 586.

4.2.6 Relief offered

It is clear that the administration order procedure does not provide for any discharge of debts or costs and that no maximum time limit for payment is set. This is contrary to international principles and guidelines which regard the discharge feature as the most important from a debt relief perspective.¹⁰⁶ Because of the lack of a discharge Roestoff submits that the procedure does not constitute an effective debt relief measure and adds that the exclusion of *in futuro* debt adds to its ineffectiveness in this regard.¹⁰⁷

The order will only lapse once all listed creditors and the cost of the administration order procedure have been paid in full.¹⁰⁸ An unintended consequence of the failure to regulate the maximum term and to make provision for a possible discharge is that a debtor may be subject to an administration order indefinitely. In this regard the Supreme Court of Appeal quoted with approval from the judgement of the court *a quo*¹⁰⁹ in *African Bank Ltd v Weiner* which held that¹¹⁰

it was never the intention of the Legislature that a debtor should be bound up indefinitely in an administration order: on the contrary, 'the mechanism of an administration order is intended to provide a debtor with a relatively short moratorium to assist in the payment of his or her debts in full and to ward off legal action and execution proceedings'.

If the intention of the legislature is indeed that which the Supreme Court of Appeal professes it to be, one cannot but wonder why the procedure does not prescribe parameters within which the repayment plan should be executed – especially since magistrates' courts are creatures of statute. Nevertheless, the procedure needs to be amended to provide for the 'twin issues' of a maximum time frame coupled with a

¹⁰⁶ See ch 2 par 2.7.

¹⁰⁷ Roestoff 'n *Kritiese evaluasie* 431.

¹⁰⁸ S 74U. This is contrary to international best practice which prescribes that procedures should not lapse in the too distant future and that rehabilitation should not be based on a certain level of repayment to creditors; ch 2 par 2.7. See Roestoff 2000 *De Jure* 132 where she proposes a prescribed term and a discharge.

¹⁰⁹ *African Bank Ltd v Weiner* (C) 575.

¹¹⁰ *African Bank Ltd v Melvyn Weiner* (SCA) 368. *Contra Fortuin v Various Creditors* 574–745 and *Ex parte August* 272–273 where it was held that the fact that the debtor has very little money and that creditors would wait for a long period to receive full payment is not a decisive factor when considering an administration procedure. Further, it was stated that neither the high court nor the legislature intended a reasonable time within which the debtor should be out of his financial embarrassment. It was further held that the legislature does not explicitly require an immediate advantage for creditors and that, if that was the intention of the procedure, it would have expressly provided as such as is the case in the Insolvency Act.

discharge of pre-administration order debt as the procedure would only in such instances result in effective relief.

4.2.7 Some comparative aspects regarding the sequestration procedure as regards debt relief

It is important to compare the different statutory debt relief procedures in order to draw inferences on the extent to which South African insolvents are, as far as it is reasonable to do so, treated similarly as the constitutionality of the position of marginalised debtors is under scrutiny.¹¹¹ It is further important to draw the comparisons in order to later ascertain whether the strengths of a particular procedure can be customised to address a weakness in another where it is appropriate to do so.

From a debt relief perspective, the administration order procedure poses advantages over and disadvantages to the sequestration procedure.¹¹² An advantage of the administration order procedure is that it was mainly created for the debtor's protection and therefore only the debtor,¹¹³ as opposed to creditors, can invoke this procedure.¹¹⁴

Another advantage for the debtor is that, as the magistrates' courts are involved in the administration order procedure, the application is much simpler and more inexpensive than the more elaborate and intricate processes of the high court.¹¹⁵ However, in this regard it is important to remember the sentiments expressed by Roper J in *Levine v Viljoen*¹¹⁶ where it was suggested that

[a]n examination of the provisions of section 74 of the Magistrates' Courts Act shows that the machinery therein provided for the administration of the estate of a debtor is of a rudimentary and limited character. On the day appointed for the hearing of an application for an administration order the debtor is obliged to appear in person and may be examined as to his financial position. There is

¹¹¹ See further par 4.4.

¹¹² See ch 3 as regards the sequestration procedure. See also Joubert 1956 *THRHR* 138–141 for a discussion of some differences in the legal consequences of the two procedures under consideration.

¹¹³ Or the court under specified circumstances; see par 4.2.1.

¹¹⁴ International guidelines do not generally favour creditor petitions due to the risk of abuse; see ch 2 para 2.6.2.3 and 2.7.

¹¹⁵ See *Bafana Finance Mabopane v Makwakwa* 586.

¹¹⁶ 1952 (1) SA 456 (W) 459.

however no provision for a systematic examination into his business transactions and his assets and liabilities such as is carried out in the case of an insolvency by the trustee of the sequestrated estate. The examination on the day of the hearing is by the presiding magistrate or by any creditor or representative of a creditor, who in the majority of cases would be unlikely to have any detailed knowledge of the affairs of the debtor as a whole, or sufficient information to form the basis of an effective inquisition into his actual financial position. There is no impounding of the applicant's books or other business records.

Simplicity and economy therefore come at the price of procedural dilution. Although this criticism by Roper J is warranted in instances where larger and more complex estates are under consideration, it is submitted that the overly involved processes found in the sequestration procedure¹¹⁷ are not appropriate where smaller, simpler estates are involved. The complex procedures for which the Insolvency Act caters are not even suited to the limited instances where the debtor would qualify for both the sequestration and the administration order procedures.¹¹⁸ In this regard, the sentiments in *Ex parte Van den Berg*¹¹⁹ is supported in that

the machinery of sequestration to distribute amongst these creditors the small amount which might be available from the sale of the immovable property after paying the costs of realisation and the costs of administration of the estate is really to use a sledgehammer to break a nut. The new machinery which has been created under the Magistrates' Courts Act is the machinery which it was intended should be used to deal with an estate of this kind – not the expensive machinery of sequestration.

A further advantage of the administration order procedure, within the realm of debt relief, is that it is not necessary to bring an application to court for rehabilitation, as is the case in sequestration proceedings (prior the point in time when automatic rehabilitation occurs) as the administrator may lodge a certificate in terms of section 74U whereupon the administration order lapses.

¹¹⁷ For instance, it makes provision for meetings of creditors and investigations into the debtor's estate.

¹¹⁸ These would theoretically be smaller estates that meet both the formal and substantive requirements of the voluntary surrender process; see ch 3 par 3.3.2.1. However, it is unthinkable that an estate that qualifies for the administration order procedure would also qualify for the sequestration procedure due to the monetary threshold that applies to the former and the advantage for creditors requirement that applies to the latter.

¹¹⁹ 1950 (1) SA 816 (W) 817.

Other comparative advantages of the administration order procedure are that a person subject to it generally retains custody and control of his estate, business and undertakings,¹²⁰ whereas most of these functions are taken over by the trustee in sequestration proceedings.

However, as regards the actual relief offered, the administration order procedure poses major disadvantages in comparison with the outcome of a sequestration procedure. The most evident advantage of the sequestration procedure is the discharge of an insolvent debtor's pre-sequestration debt upon rehabilitation. No such discharge exists under the administration order procedure. Closely related to this aspect is the fact that a person may technically be subject to an administration order indefinitely. In turn, a person under sequestration can, under certain circumstances and on application to court, be rehabilitated immediately after the master's confirmation of the distribution account. In other instances the debtor may generally apply for his rehabilitation before the ten-year period, after which automatic rehabilitation takes place, has expired.

4.2.8 Reform proposals and initiatives

In July 2000, the Department of Justice and Constitutional Development and the Law Society of South Africa requested the Centre for Advanced Corporate and Insolvency Law at the University of Pretoria to investigate the reform of the administration order procedure. The research results were incorporated in a report submitted to the Department of Justice and Constitutional Development in May 2002. The matter was referred to the South African Law Reform Commission for investigation, and a reform project was registered as Project 127.

The reform project was suspended, pending the promulgation of the NCA. However, contrary to expectations, the NCA did not deal with the administration order procedure, and on 1 May 2011 a workshop was held at the University of Pretoria where various interest groups were consulted on proposed amendments to the process. The suggested amendments mainly focus on technical and procedural

¹²⁰ However, as was discussed in par 4.2.1, the administration order procedure may take the form of a hybrid measure as, in some instances, assets may be liquidated to service debt.

aspects. However, a discharge after eight years, subject to specified conditions, is proposed – which is certainly a step in the right direction as far as relief offered is concerned.¹²¹

4.3 Aspects of the debt review procedure

4.3.1 Application of the NCA

As was stated above, section 86 of the NCA provides for a specific debt relief measure known as debt review. This process is in practice sometimes loosely referred to as debt counselling. However, the NCA only regulates certain specified types of civil obligations, collectively termed credit agreements, as defined in the NCA.¹²² Furthermore, even if an obligation strictly falls within the definition of a specific type of credit agreement, the NCA will in certain circumstances not apply to such an agreement as the application thereof may be specifically excluded. In other instances the NCA has only limited application. It is imperative to ascertain the exact scope of application of the NCA and specifically which debts may be included in the debt review procedure as consumers with other types of debt will not be able to obtain the relief that the NCA provides. It is also important to determine the extent of application of the NCA's reckless credit provisions as they may in some instances be used as a tool in the debt restructuring process.¹²³

Even though the NCA itself limits its scope as will be seen below, the parties to an agreement to which the NCA applies cannot agree to exclude its application to their agreement.¹²⁴ The other side of the coin, namely, whether it is permissible for parties to a credit agreement to render the NCA applicable under circumstances where, in terms of its own provisions, it does not apply to the agreement has been the subject of contradicting judgments.¹²⁵ Although the issue has not been finally settled by the courts, it is submitted that it is possible to incorporate provisions of the NCA into a

¹²¹ See the proposed amendment to ss 74U and 74(1A)(d); workshop documents on file with the author.

¹²² See Stoop 2008 *De Jure* 352 for a detailed discussion of the application of the NCA. See also Van Zyl 'Scope of application of the National Credit Act' ch 4; Otto 'Types of credit agreement' ch 8; Otto and Otto *NCA explained* ch 3 and Kelly-Louw and Stoop *Consumer credit regulation* ch 2.

¹²³ Reckless credit in terms of the NCA is discussed in ch 5 par 5.5.

¹²⁴ S 90(2)(b).

¹²⁵ See *First National Bank v Clear Creek Trading 12 (Pty) Ltd* 2014 (1) SA 23 (GNP) where the question was answered in the affirmative. However, the court in *RMB Private Bank v Kaydeez Therapies CC* 2013 (6) SA 308 (GSJ) reached an opposite conclusion.

credit agreement, in accordance with the principles of incorporation by reference, but that it will only apply to the parties to the agreement.¹²⁶

Unlike its predecessors, namely, the Usury Act¹²⁷ and the Credit Agreements Act,¹²⁸ the NCA's protective measures prescribe no artificial monetary ceiling as far as natural persons are concerned,¹²⁹ and include credit agreements relating to all goods and services.

Section 4 regulates the general application of the NCA and section 4(1) provides that the NCA applies to every credit agreement between parties dealing at arm's length made within or having an effect within the Republic. From this subsection it is clear that three general requirements should be present before the NCA will apply. The agreement should (i) be classified as a credit agreement;¹³⁰ (ii) the parties should be dealing at arm's length; and (iii) the agreement must have been concluded or at least have an effect within the Republic. A fourth requirement not mentioned in section 4(1) should be added, namely, that no exclusions must be applicable. These requirements are considered in more detail below.

An agreement constitutes a credit agreement if it qualifies as a credit facility, credit transaction, credit guarantee or a combination thereof.¹³¹ An agreement will be a credit facility¹³² if a credit provider supplies goods, services or money to a consumer from time to time¹³³ and either defers the consumer's obligation to pay any part of the cost of goods, services or money or bills the consumer periodically.¹³⁴ A further

¹²⁶ See in general Renke and Coetzee 2014 *THRHR* 567. See also *First National Bank v Clear Creek Trading 12 (Pty) Ltd* [2015] ZASCA of 9 March 2015. The decision unfortunately did not provide a decisive answer.

¹²⁷ 73 of 1968.

¹²⁸ 75 of 1980.

¹²⁹ Monetary caps are applicable to juristic persons. See, eg, s 4(1)(a).

¹³⁰ It was held that the charging of interest, levies, rates and taxes relating to legislation does not fall within the ambit of the NCA. See *Mitchell v Beheerliggaam RNS Mansions* 2010 (5) SA 75 (GNP) 81 and *Nelson Mandela Bay Metropolitan Municipality v Nobumba* 2010 (1) SA 579 (ECG) 590. For a discussion of the last case see Otto 2011 *De Jure* 10. It was also held that the NCA does not apply to an acknowledgement of debt based on a damage claim; *Grainco (Pty) Ltd v Broodryk* 2012 (4) SA 517 (FB) 524.

¹³¹ S 8(1).

¹³² S 8(3).

¹³³ S 8(3)(a)(i).

¹³⁴ S 8(3)(a)(ii).

prerequisite to qualify as a credit facility is that a charge, fee or interest is added to the amount deferred or periodically billed to the consumer.¹³⁵ This type of credit agreement can generally be described as revolving credit and examples are credit cards, overdrafts on cheque accounts or store cards.¹³⁶

An agreement constitutes a credit guarantee¹³⁷ if a person undertakes or promises to satisfy upon demand any obligation of another consumer in terms of a credit facility or a credit transaction to which the NCA applies. This is commonly known as a suretyship.¹³⁸

In turn, an agreement will be a credit transaction¹³⁹ if the agreement constitutes a pawn transaction,¹⁴⁰ discount transaction,¹⁴¹ incidental credit agreement,¹⁴²

¹³⁵ S 8(3)(b).

¹³⁶ See for instance *JMV Textiles (Pty) Ltd v De Chalain Spareinvest 14 CC 2010 (6) SA 173 (KZD)* 179 where Wallis J states that s 8(3) is directed at charge cards and credit cards and not at conventional credit sales.

¹³⁷ S 8(5).

¹³⁸ See *FirstRand Bank Ltd v Carl Beck Estates (Pty) Ltd 2009 (3) SA 384 (T) 390*. See also Otto and Otto *NCA explained* 9.4 and Stoop and Kelly-Louw 2011 *PELJ* 67.

¹³⁹ S 8(4).

¹⁴⁰ A pawn transaction is an agreement in terms of which a creditor advances money or extends credit and at the same time takes possession of goods as security for the money advanced or credit granted. Either the estimated resale value of the goods must exceed the value of the money provided or credit extended or a charge, fee or interest must be imposed in respect of the agreement, the loaned amount or the credit extended. The credit provider is entitled, after a specified period, to sell the goods and retain the proceeds of the sale in settlement of the consumer's obligations under the agreement if the consumer fails to satisfy the obligation; s 1. Certain provisions of the NCA are not applicable to pawn transactions, eg, unlawful agreements in terms of s 89(1) and reckless credit in terms of s 78(2).

¹⁴¹ In a discount transaction, goods or services are provided to a consumer over a period of time and more than one price is quoted. A lower price applies if the account is paid on or before a determined date and a higher price if paid after the determined date or periodically; s 1.

¹⁴² Incidental credit is extended where an account is tendered for goods or services that have been provided to a consumer, or are to be provided to a consumer over a period of time and a fee, charge or interest is payable when payment is not made on or before a specified date. Where two prices are quoted for settlement of an account (the lower if the account is paid on or before a specified date, and the higher if the account is not paid by that date), the agreement will also constitute an incidental credit agreement; s 1. There is an obvious overlap between the definitions of incidental credit and a discount transaction. It is submitted that the legislature should intervene to clarify this issue. In terms of section 5(2) incidental credit agreements are deemed to have been made:

Twenty business days after (a) the supplier of the goods or services that are the subject of that account, first charges a late payment fee or interest in respect of that account; or (b) a pre-determined higher price for full settlement of the account first becomes applicable, unless the consumer has fully paid the settlement value before that date.

instalment agreement,¹⁴³ mortgage agreement,¹⁴⁴ secured loan¹⁴⁵ or a lease of movable property.¹⁴⁶

When an agreement does not fall in one of the credit transaction categories discussed above and where it cannot be classified as revolving credit (credit facility) or a suretyship (credit guarantee), it will still constitute a credit transaction if the agreement is characterised by a deferral of payment and the levying of a charge, fee or interest.¹⁴⁷

The NCA also applies to a combination of a credit transaction, a credit facility and a credit guarantee.¹⁴⁸ An example is where a consumer enters into an instalment agreement and payments are effected through the budget option on a credit card.¹⁴⁹ From the description of the various forms of credit agreements it can be seen that, generally, credit agreements have two characteristics – a deferral of payment¹⁵⁰ and costs, fees or charges that are added to the agreement.¹⁵¹

¹⁴³ An instalment agreement is an agreement where movable property is sold to a consumer and all or part of the price of such property is deferred and is to be paid through instalments. Possession and use of the property are immediately transferred to the consumer, but ownership passes (a) when the agreement has been fully complied with; or (b) immediately subject to a right of re-possession should the consumer fail to meet his financial obligations under the agreement. Interest, fees or other charges are payable in respect of the agreement, or the amount so deferred; s 1. The spelling of the word 'instalment' in the NCA is not correct according to UK English used in this thesis. Although the incorrect spelling is recognised, preference is given to the spelling used in the NCA.

¹⁴⁴ A mortgage agreement is defined as 'a credit agreement that is secured by the registration of a mortgage bond by the registrar of deeds over immovable property'. The definition was amended by s 1 of the Amendment Act.

¹⁴⁵ A secured loan is an agreement in terms of which a credit provider advances money or extends credit to a consumer and retains, or receives a pledge to any movable property or other thing of value as security for amounts outstanding under the agreement. Instalment agreements are specifically excluded from the definition of secured loans; s 1. The definition was amended by s 1 of the Amendment Act.

¹⁴⁶ An agreement can be typified as a lease of movable property if movable goods are let to the consumer. Payment is made on a periodic basis or deferred for a period and interest and fees or other charges are payable. Ownership of the property passes to the consumer absolutely or upon fulfilment of specific conditions at the end of the term; s 1. There is a clear overlap between the definitions of instalment agreement and lease of movable property. It is submitted that the legislature should intervene to clarify this issue.

¹⁴⁷ S 8(4)(f). A wide interpretation is given to the terms 'fee', 'charge' and 'interest' including any consideration payable in respect of a credit agreement, irrespective of the wording attached thereto; *Evans v Smith* 2011 (4) SA 472 (WCC) 479–480.

¹⁴⁸ S 8(1)(d).

¹⁴⁹ *Otto and Otto NCA explained* 9.5.

¹⁵⁰ Or prepayment of debt in case of a discount transaction or incidental credit agreement.

¹⁵¹ See *Renke et al 2007 Obiter* 235 and *Otto and Otto NCA explained* 8. It should be pointed out that the NCA in certain instances defines agreements as developmental (s 10) or public interest

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The second general requirement for the NCA to apply to a credit agreement is that parties should be dealing at arm's length. Even though this concept is not defined, the NCA provides a few examples of agreements where parties will not be dealing at arm's length.¹⁵² In these instances the NCA therefore does not apply. For instance, a credit agreement between natural persons who are in a familial relationship and are co-dependent upon one another or where one is dependent on the other¹⁵³ or where the parties are not independent and do not strive to obtain the utmost advantage out of the transaction constitute arm's length transactions.¹⁵⁴

The last general requirement is that the NCA will apply where the agreement was concluded in South Africa or has an effect within the Republic.¹⁵⁵ In this instance, the legislature specifically ousted the common-law presumption that legislation does not have extraterritorial application.¹⁵⁶

However, even if an agreement can be classified as a credit agreement according to the definitions of credit facility, credit transaction or credit guarantee, and it adheres to the other general requirements, it will not be regulated by the NCA if it is specifically excluded from the ambit thereof. The NCA excludes the following agreements as they are not deemed to be credit agreements:

- a. an insurance policy (or credit extended for maintaining the premiums on an insurance policy);¹⁵⁷
- b. a lease of immovable property;¹⁵⁸ and
- c. a transaction between a stokvel and its members.¹⁵⁹

(s 11) credit agreements. These agreements can be characterised as altruistic agreements and enjoy special privileges in terms of the NCA. Although both types are subject to the debt review provisions in the NCA, the provisions regarding reckless credit do not apply to them.

¹⁵² S 4(2)(b).

¹⁵³ S 4(2)(b)(iii).

¹⁵⁴ S 4(2)(b)(iv)(aa).

¹⁵⁵ S 4(1).

¹⁵⁶ Whether a credit agreement has effect in the Republic will depend on the circumstances of the particular agreement and must be determined on the specific facts present; Van Zyl 'Scope of application of the National Credit Act' 4.2.

¹⁵⁷ S 8(2)(a).

¹⁵⁸ S 8(2)(b).

¹⁵⁹ S 8(2)(c). A stokvel is defined in s 1 as

a formal or informal rotating financial scheme with entertainment, social or economical functions, which (a) consists of two or more persons in a voluntary association, each of whom has pledged mutual support to the others towards the attainment of specific objectives; (b) establishes a continuous pool of capital by raising funds by means of the subscriptions of the

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Furthermore, the debt resulting from a dishonoured cheque or similar instrument does not constitute a credit agreement for purposes of the NCA.¹⁶⁰ Similarly, when payment takes place through a charge against a credit facility (for example a credit card where a third party is the credit provider) and such a charge is refused by the credit provider for any reason, the resulting debt does not constitute a credit agreement in terms of the NCA.¹⁶¹

A debt arising from a continuous service¹⁶² may also be an exemption in terms of the NCA. In the event that a supplier of a utility¹⁶³ or other continuous service defers payment until an account has been rendered and the supplier does not impose any charge in respect of the amount so deferred if the consumer pays before a certain period, the agreement will not qualify as a credit facility.¹⁶⁴ The consumer must be given at least 30 business days¹⁶⁵ after the account has been rendered to settle same.¹⁶⁶ Any overdue amount on which interest is charged will be deemed to be incidental credit.¹⁶⁷ It seems that continuous services have been exempted in order to exclude the application of the NCA to agreements between municipalities and consumers, although other service providers may also construct their agreements to fall within this exemption.¹⁶⁸

members; (c) grants credit to and on behalf of members; (d) provides for members to share in profits from, and to nominate management of, the scheme; and (e) relies on self-imposed regulation to protect the interest of its members.

¹⁶⁰ S 4(5).

¹⁶¹ S 4(5)(b).

¹⁶² Continuous service is defined in s 1 as

the supply for consideration of a utility or service, other than credit or access to credit, or the supply of such a utility or service combined with the supply of any goods that are essential for the utilisation of that utility or service by the consumer, with the intent that, so long as the agreement to supply that utility or service remains in force, the supplier will make the service continuously available to be used, accessed or drawn upon (a) from time to time as determined by the consumer; and (b) with any frequency or in any amount as determined, accessed, required, demanded or drawn upon by the consumer, subject only to any total use or cost limits set out in the agreement.

¹⁶³ Utility is defined in s 1 as

the supply to the public of an essential (a) commodity, such as electricity, water, or gas; or (b) service, such as waste removal, or access to sewage lines, telecommunication networks or any transportation infrastructure.

¹⁶⁴ S 4(6)(b). See *Nelson Mandela Bay Metropolitan Municipality v Nobumba* for an exposition of the section.

¹⁶⁵ According to s 2(5) the number of business days is calculated by excluding the first day on which an event occurs and including the day on which the second occurs. Public holidays, Saturdays and Sundays that fall on or between these days are excluded.

¹⁶⁶ S 4(6)(b)(ii).

¹⁶⁷ S 4(6)(b)(ii).

¹⁶⁸ Van Zyl 'Scope of application of the National Credit Act' 4.3.

As the legislature is of the opinion that certain other consumers are not in need of the NCA's protection, further exclusions are provided for. This is in spite of the fact that the agreements these consumers enter into comply with the other requirements discussed above in order for the NCA to apply. The most important exclusion involves juristic persons¹⁶⁹ where they act in their capacity as consumers.¹⁷⁰ Even where the NCA applies to certain juristic person consumers, it only has limited application. The NCA further has limited application to incidental credit agreements, credit guarantees, school or student loans,¹⁷¹ emergency loans,¹⁷² public interest credit agreements, pawn transactions, a temporary increase in the credit limit under a credit facility¹⁷³ and pre-existing credit agreements. It is important to note that, although the provisions relating to credit assessments and reckless credit do not apply to incidental credit agreements, the remainder of chapter 4 part D, including the debt review provisions of the NCA, apply to such agreements.¹⁷⁴

¹⁶⁹ S 1 of the NCA defines a juristic person as including a partnership, association or other body of persons, corporate or unincorporated, or a trust if

- (a) there are three or more individual trustees; or
- (b) the trustee is itself a juristic person, but does not include a stokvel;

¹⁷⁰ S 4(1). This thesis is not concerned with debt relief relating to juristic persons and therefore does not consider provisions relating to them in detail.

¹⁷¹ A school loan is defined in s 1 as a credit agreement in terms of which

- (a) money is paid to a primary or secondary school on account of school fees or related costs for the benefit of the consumer's child or other dependant; or
- (b) a primary or secondary school defers payment of all or part of the school fees or related costs for the consumer's child or other dependant.

A student loan is defined in s 1 as a credit agreement in terms of which

- (a) money is paid by the credit provider to an institution of tertiary education on account of education fees or related costs for the benefit of the consumer or a dependant of the consumer; or
- (b) an institution of tertiary education defers payment of all or part of the consumer's education fees or related costs;

¹⁷² Emergency loan is defined in s 1 as a credit agreement entered into by a consumer to finance costs arising from or associated with

- (a) a death, illness or medical condition;
- (b) unexpected loss or interruption of income; or
- (c) catastrophic loss of or damage to home or property due to fire, theft, or natural disaster, affecting the consumer, a person who is dependent upon the consumer or a person for whom the consumer is financially responsible.

¹⁷³ S 119.

¹⁷⁴ S 5(1) deals with the parts of the NCA that do not apply to incidental credit agreements.

Although this thesis is not concerned with debt relief relating to juristic persons, it is noted for completeness sake that the whole of chapter 4 part D of the NCA does not apply to those juristic persons who are subject to the NCA as consumers.¹⁷⁵

As far as the NCA's limited application to credit guarantees is concerned, it will only apply to a credit guarantee to the extent that it is applicable to the credit transaction or credit facility in respect of which the guarantee is granted.¹⁷⁶ Chapter 4 part D will therefore not apply to a suretyship entered into by a natural person where the NCA does not apply to the principal agreement.¹⁷⁷

The reckless credit provisions in terms of the NCA do not apply to school or student loans, emergency loans, public interest credit agreements,¹⁷⁸ pawn transactions and a temporary increase in the credit limit under a credit facility. However, these debts may be included in the debt review process.¹⁷⁹

Many credit agreements that were entered into prior to the commencement of the NCA will still be in force long after its effective date, such as mortgage agreements. Schedule 3 item 4 sets out the extent to which the NCA applies to pre-existing credit agreements. Item 4(1) provides that as a point of departure all agreements that would have been subject to the NCA, had the NCA been in force when the agreements were entered into, will be subject to the NCA. Certain provisions are fully applicable, others have limited application and some are not applicable at all. However, relevant to this discussion is that chapter 4 part D applies to pre-existing

¹⁷⁵ S 6.

¹⁷⁶ S 4(2)(c). See Van Zyl 'Scope of application of the National Credit Act' 4.4.3.

¹⁷⁷ See *FirstRand Bank Ltd v Carl Beck Estates (Pty) Ltd* 390; *Nedbank Ltd v Wizard Holdings (Pty) Ltd* 2010 (5) SA 523 (GSJ) 526; *Structured Mezzanine Investments (Pty) Ltd v Davids* 2010 (6) SA 622 (WCC) 628; *Ribeiro v Slip Knot Inv 777 (Pty) Ltd* 2011 (1) SA 575 (SCA) 580. In *Standard Bank of SA v Hunkydory Investments 194 (Pty) Ltd* 2010 (1) SA 627 (C) it was contended that s 4(2) is unconstitutional as it protects sureties of natural persons but not of large juristic persons or juristic persons entering into large agreements. The court found that it was not the case; 633.

¹⁷⁸ In order for the reckless credit provisions not to be applicable to the preceding four categories, s 78(2) contains the proviso that such agreements must be reported to the national credit register in the prescribed manner and form. See also reg 23. In respect of an emergency loan, reasonable proof of an emergency as defined in s 1 should be obtained and retained by the credit provider. S 1 refers to death, illness or medical condition, unexpected loss or interruption of income or catastrophic loss of or damage to home or property due to fire, theft or natural disaster affecting the consumer and his dependants as emergencies in this regard.

¹⁷⁹ S 78(2).

agreements only to the extent that they do not concern reckless credit.¹⁸⁰ Such agreements may therefore be included in an application for debt review.

4.3.2 Overview of and general commentary on the process

One of the aims of the NCA is to provide for debt relief through debt re-organisation in cases of over-indebtedness.¹⁸¹ However, contrary to international principles and guidelines,¹⁸² the Act does not strive to address over-indebtedness by providing a discharge of debt to over-indebted consumers.¹⁸³ In this regard the Supreme Court of Appeal in *Collett v FirstRand Bank Ltd*¹⁸⁴ recently stated that:

The purpose of the debt review is not to relieve the consumer of his obligations, but to achieve either a voluntary debt re-arrangement or a debt re-arrangement by the magistrates' (sic) court.

As was seen in the discussion above, the NCA regulates a very specific sector of the credit industry. It only applies to credit agreements as defined by the NCA and provides protection to certain debtors only.¹⁸⁵ Where a natural person consumer finds himself in financial distress and a significant portion of his debt relates to credit agreements as regulated by the NCA, such a debtor may consider applying for debt review in terms of section 86.¹⁸⁶

¹⁸⁰ Item 4(2).

¹⁸¹ See the preamble to the NCA. See also *FirstRand Bank Ltd v Olivier* 2009 (3) SA 353 (SE) 357 and *Otto* 2009 SA *Merc LJ* 272 for a discussion of the case. See further *Standard Bank of SA Ltd v Panayiotis* 2009 (3) SA 363 (W) 375.

¹⁸² Ch 2 par 2.7.

¹⁸³ See s 3(g) and (i).

¹⁸⁴ 2011 (4) SA 508 (SCA) 514. See also *Ex parte Ford* 2009 (3) SA 376 (WCC) 383.

¹⁸⁵ See par 4.3.1.

¹⁸⁶ S 86 should be read with the National Credit Regulations, 2006 (hereafter 'the regulations'), ch 3 pt D and Debt Counselling Regulations, 2012. See also the Credit Industry Forum *Task team agreement* (available at www.ncr.org) which presents standardised norms with the aim of addressing operational and procedural weaknesses of the debt review procedure. It further promotes a uniform and consistent approach amongst all stakeholders; 1. Such standardisation is in line with international best practice; see ch 2 par 2.7. For a detailed discussion of the debt review process see Roestoff *et al* 2009 *PELJ* 255 *et seq*; Boraine *et al* 2012 *De Jure* 93–103; Boraine and Roestoff 2014 *THRHR* 358 *et seq*; Van Heerden 'Over-indebtedness and reckless credit' 11.3.3.2 and 'A practical discussion of the debt-counselling process' ch 14 and *Otto and Otto NCA explained* 30.9.

The debt review process commences with a consumer applying to a debt counsellor¹⁸⁷ to have him declared over-indebted.¹⁸⁸ Debt counsellors are registered¹⁸⁹ at and strictly regulated by the NCR.¹⁹⁰ Once an application has been made, credit providers may not proceed to take steps to enforce their rights under credit agreements.¹⁹¹ This preclusion goes both ways as an application for debt review may not include a credit agreement where

the credit provider under that credit agreement has proceeded to take the steps contemplated in section 130 to enforce that agreement.¹⁹²

However, it is possible for an over-indebted consumer to raise his over-indebtedness after steps to enforce the agreement had been taken by the credit provider by making use of the provisions as set out in section 85.¹⁹³ The section provides that

[d]espite any provision of law or agreement to the contrary, in any court proceedings in which a credit agreement is being considered, if it is alleged that the consumer under a credit agreement is over-indebted, the court may

(a) refer the matter directly to a debt counsellor with a request that the debt counsellor evaluate the consumer's circumstances and make a recommendation to the court in terms of section 86(7); or

¹⁸⁷ A debt counsellor is defined in the regulations as 'a neutral person who is registered in terms of s 44 of the Act offering a service of debt counselling'. Only natural persons may be registered as debt counsellors and an unregistered person may not offer or engage in the services of a debt counsellor in terms of the NCA; s 44(1) and (2). Debt counsellors need to adhere to criteria for registration relating to education, experience and competence (see reg 10). Further, as regards the application, the consumer applies for the debt review procedure by submitting a completed form 16 (all forms are contained in sch 1 of the regulations) or a list of information to the debt counsellor. Specified documents must also be submitted to the debt counsellor and the prescribed fee must be paid; reg 24(1). See *BMW Financial Services (SA) (Pty) Ltd v Donkin* 2009 (6) SA 63 (KZD) where the moment of application for debt review was considered and the discussion of the case by Van Heerden and Coetzee 2010 *Obiter* 756.

¹⁸⁸ S 86(1) read together with reg 24(1).

¹⁸⁹ See pts A and C of ch 2 of the regulations.

¹⁹⁰ Hereafter the 'NCR'. The NCR is an independent statutory body established through the NCA. The NCR is only subject to the Constitution of the Republic of South Africa, 1996 and the law; s 12.

¹⁹¹ S 88(3). The moratorium takes effect at an appropriate time; see ch 2 par 2.7.

¹⁹² S 86(2). See par 4.3.3 for a discussion of the section and case law decided in terms thereof. See in particular the discussion of *Sebola v Standard Bank of South Africa Ltd* 2012 (5) SA 142 (CC) and *Kubyana v Standard Bank of South Africa Ltd* 2014 (3) SA 56 (CC). These cases were decided on s 86(2) before its amendment in terms of s 26(a) of the Amendment Act that substituted the referral to s 129 with a referral to s 130. A debt review will therefore be competent in respect of a specific agreement even where a s 129(1)(a) notice has been delivered to the consumer. A question which arises in light of the amendment is at what moment a specific agreement will now be excluded from the debt review procedure and more specifically whether it is the issuing or the service of a summons that will exclude such an agreement. It is submitted that it is the service of the summons; see Coetzee *Impact* 86–87 *et seq.*

¹⁹³ This section is discussed in detail in ch 5 par 5.4. See Kreuser 2012 *De Jure* 1 and Van Heerden 2013 *De Jure* 968 for detailed discussions of s 85.

- (b) declare that the consumer is over-indebted, as determined in accordance with this Part, and make any order contemplated in section 87 to relieve the consumer's over-indebtedness.

On receipt of the application for debt review, the debt counsellor may require the consumer to pay an application fee¹⁹⁴ before accepting the application. However, a debt counsellor may not require or accept a fee from a credit provider in respect of such an application.¹⁹⁵

The debt counsellor must provide the consumer with proof of receipt of the application and must notify all credit providers listed in the application and every registered credit bureau.¹⁹⁶ It is important to note that the consumer and every credit provider that received a notice of the application must comply with reasonable requests by the debt counsellor to enable the assessment of the consumer's state of indebtedness and the prospects of reasonable debt re-arrangement. They must further participate in good faith in the review and in negotiations intended to result in responsible debt re-arrangement.¹⁹⁷

There are conflicting judgments relating to the consequences of a credit provider's failure to participate in good faith in the debt review process. Some judgments held

¹⁹⁴ S 86(3)(a). The fee is R50; sch 2 of the regulations. As the amount is obviously not sufficient to render debt counselling services, the Debt Counsellors Association of South Africa (DCASA) suggested a fee structure or guideline that was approved by the NCR. See www.ncr.org as regards the latest fee structure.

¹⁹⁵ S 86(3)(b). The consumer is responsible for all debt counselling fees, which is contrary to international consensus that all parties that benefit from the system should contribute and that costs should not constitute an access barrier; see ch 2 par 2.7.

¹⁹⁶ S 86(4). The notification takes place by providing a completed form 17.1 to credit providers and credit bureaus by fax, registered mail or email, within 5 business days after receiving the debt review application. The debt counsellor must keep a record of delivery thereof; reg 24(2) and (5). The debt counsellor must verify the information provided by the consumer by requesting documentary proof from the consumer, relevant credit providers or the employer or by any other means; reg 24(3). If the credit provider does not provide the requested information within five business days, the debt counsellor may accept the information as provided by the consumer as correct; reg 24(4).

¹⁹⁷ S 86(5). See *Collett v FirstRand Bank* 516 where it was held that the duty to negotiate does not terminate after the proposal has been referred to the magistrate's court, but continues pending the hearing. In *Ferris v FirstRand Bank Ltd* 2014 (3) SA 39 (CC) 46 it was held that the good faith requirement only becomes irrelevant when a debt-restructuring order is granted. See also *Seyffert v FirstRand Bank* 2012 (6) SA 581 (SCA) 585. For a discussion of the case within the context of execution against mortgaged homes see Steyn 2012 *De Jure* 639. See further Van Heerden 'Over-indebtedness and reckless credit' 11.3.3.2 regarding the 'good faith' requirement.

that the NCA does not sanction such failure,¹⁹⁸ whilst others read in a sanction for non-compliance.¹⁹⁹ Whether a credit provider has adhered to the good faith requirement is a factual inquiry.²⁰⁰ However, good faith is also required from the debt counsellor and the consumer.²⁰¹ It was remarked in *SA Taxi Securitisation (Pty) Ltd v Ndobela*²⁰² that '[i]t is a reciprocal duty on both parties to engage meaningfully in a (sic) debt review negotiations'.

After a debt counsellor has accepted the consumer's application, he must determine whether the consumer appears to be over-indebted²⁰³ and, where the consumer also

¹⁹⁸ See *SA Taxi Securitisation (Pty) Ltd v Mbatha* 2011 (1) SA 310 (GSJ) 322 where it was stated that the credit provider's right to terminate a debt review is not reliant on the obligation to act in good faith.

¹⁹⁹ In *FirstRand Bank Ltd v Raheman* 2012 (3) SA 418 (KZD) 421–422 the defendants raised the issue that the plaintiff's failure to respond to their debt counsellor's proposal was reckless and that a punitive cost order should be given against them. Mokgohloa J agreed that s 85 requires good faith from both parties in the review and any negotiations designed to result in responsible debt rearrangements and stated that should the credit provider fail in this regard the court may order, on request by the consumer, that the debt review resume. However, no such request was made by the defendants as there was already a debt review order in place. The judge continued by stating that the plaintiff's failure to participate was reckless, but not to an extent of attracting a punitive cost order against it. It therefore seems that the court is of the opinion that punitive costs could be awarded in such circumstances. See *Mercedes Benz Financial Services South Africa (Pty) Ltd v Dunga* 2011 (1) SA 374 (WCC) 379 where the court found it necessary to imply a proviso to section 86(10), namely, that it is not prudent for a credit provider to terminate a debt review where he did not act in good faith. See also *Wesbank Ltd v Papier* 2011 (2) SA 395 (WCC) 404.

²⁰⁰ See Van Heerden 'Over-indebtedness and reckless credit' 11.3.3.2 and authorities cited there.

²⁰¹ See *FirstRand Bank Ltd v Mvelase* 2011 (1) SA 470 (KZP) in general and specifically 487–489.

²⁰² [2011] ZAGPJHC of 15 March 2011 par 22.

²⁰³ In terms of s 79(1)

[a] consumer is over-indebted if the preponderance of available information at the time a determination is made indicates that the particular consumer is or will be unable to satisfy in a timely manner all the obligations under all the credit agreements to which the consumer is a party, having regard to that consumer's

(a) financial means, prospects and obligations; and

(b) probable propensity to satisfy in a timely manner all the obligations under all the credit agreements to which the consumer is a party, as indicated by the consumer's history of debt repayment.

Reg 24(7) provides that the debt counsellor should take cognisance of s 79 when making the assessment and must further consider the following:

(a) A consumer is over-indebted if his/her total monthly debt payments exceed the balance derived by deducting his/her minimum living expenses from his/her net income;

(b) Net income is calculated by deducting from the gross income, statutory deductions and other deductions that are made as a condition of employment;

(c) Minimum living expenses are based upon a budget provided by the consumer, adjusted by the debt counsellor with reference to guidelines issued by the National Credit Regulator.

As regards general standards in relation to living expenses refer to the Credit Industry Forum *Task team agreement* (available at www.ncr.org).

'[F]inancial means, prospects and obligations' for purposes of ch 4 pt D and in accordance with s 78(3) include

Footnote continues on next page

seeks a declaration of reckless credit, whether any of the agreements appear to have been recklessly entered into.²⁰⁴ This determination must take place within 30 business days from the date on which the application was received by the debt counsellor²⁰⁵ whereafter he must notify affected credit providers and registered credit bureaus of the outcome.²⁰⁶ Depending on the outcome of the assessment, the NCA prescribes three different courses of action that the debt counsellor should take.²⁰⁷ If the consumer is found not to be over-indebted, the debt counsellor must reject the application, even where a particular agreement was found to be recklessly concluded.²⁰⁸ Where the debt counsellor found that the consumer is not over-indebted but is experiencing or is likely to experience difficulty in satisfying all his obligations under all his credit agreements timeously, the debt counsellor may

-
- (a) income, or any right to receive income, regardless of the source, frequency or regularity of that income, other than income that the consumer or prospective consumer receives, has a right to receive, or holds in trust for another person;
 - (b) the financial means, prospects and obligations of any other adult person within the consumer's immediate family or household, to the extent that the consumer, or prospective consumer, and that other person customarily –
 - (i) share their respective financial means; and
 - (ii) mutually bear their respective financial obligations; and
 - (c) if the consumer has or had a commercial purpose for applying for or entering into a particular credit agreement, the reasonably estimated future revenue flow from that business purpose.

A determination of over-indebtedness should consider the above factors as they exist at the time of the determination; s 79(2). However, over-indebtedness also relate to future inability, hence 'or will be unable to satisfy' in s 79(1). S 79(3) provides that when making the determination, the value of a credit facility is the settlement value at that time and the value of a guarantee is the settlement value of the agreement that it guarantees if the guarantor has been called upon to honour the guarantee or the settlement value of the agreement that it guarantees, discounted by a prescribed factor. In *Standard Bank v Panayiotts* 374–375 it was held that the determination of over-indebtedness included the prospect of improving the financial situation by liquidating assets. See also Boraine *et al* 2012 *De Jure* 94. The NCA makes use of, amongst others, the liquidity test as an access requirement which is in line with international principles and guidelines; ch 2 par 2.7.

²⁰⁴ S 86(6)(b). Reg 24(8) provides that the debt counsellor should consider s 80 of the NCA when making a determination on whether a particular agreement is reckless and further factors included in the specific regulation. See further ch 5 par 5.5.

²⁰⁵ Reg 24(6).

²⁰⁶ The notification takes place by providing a completed form 17.2 within five business days of the assessment; reg 24(10).

²⁰⁷ S 86(7).

²⁰⁸ S 86(7)(a). Reg 25 determines that the debt counsellor must provide the consumer with a letter of rejection that contains information as set out in the specific regulation. In terms of s 86(9), the consumer, with leave of the magistrate's court may apply directly for an order that the consumer is over-indebted and the relevant subsequent orders. According to reg 26 such application must be made within 20 business days, and by making use of form 18, after the debt counsellor has provided the letter of rejection. This period may be extended by the court on good cause shown; reg 26(2). See also reg 4 of the Debt Counselling Regulations, 2012 that, amongst others, provides that an application in terms of s 86(9) should be lodged in the manner and form prescribed by rule 55 of the Magistrates' Courts Rules.

recommend that the consumer and the respective credit providers voluntarily consider and agree on a plan of debt re-arrangement.²⁰⁹ The third course of action is more relevant to this discussion and should be taken where the consumer is found to be over-indebted.²¹⁰ In such an instance the debt counsellor may issue a proposal²¹¹ recommending that the magistrate's court make one or both of two orders. The first is an order to declare agreements that the debt counsellor found to be reckless, as such.²¹² The second is that one or more of the consumer's obligations are re-arranged by²¹³

- (aa) extending the period of the agreement and reducing the amount of each payment due accordingly;
- (bb) postponing during a specified period the dates on which payments are due under the agreement;
- (cc) extending the period of the agreement and postponing during a specified period the dates on which payments are due under the agreement; or
- (dd) recalculating the consumer's obligations because of contraventions of Part A²¹⁴ or B²¹⁵ of Chapter 5 or Part A²¹⁶ of Chapter 6.

Van Heerden notes that, in practice, debt counsellors as a matter of course first approach credit providers with voluntary proposals before approaching the court for an order.²¹⁷

Section 87 contains the court's powers when re-arranging a consumer's obligations. The section provides as follows:

²⁰⁹ S 86(7)(b). This was referred to as 'a voluntary rearrangement' by the court in *National Credit Regulator v Nedbank Ltd* 2009 (6) SA 295 (GNP) 301.

²¹⁰ S 86(7)(c).

²¹¹ Reg 2 of the Debt Counselling Regulations, 2012 provides that such a proposal must take the form of an application and must be lodged in a manner and form prescribed by rule 55 of the Magistrates' Courts Rules.

²¹² S 86(7)(c)(i).

²¹³ S 86(7)(c)(ii). In *National Credit Regulator v Nedbank Ltd* 302 the court referred to this scenario as 'a rearrangement by the court'. As was noted above, the debt review procedure does not directly require that assets should be used to service debt although debt counsellors should consider such measures when assessing a consumer's financial situation. This is in line with international principles and guidelines in that a debtor must do the best that he can to service his debts; see ch 2 par 2.7.

²¹⁴ Ch 5 pt A deals with unlawful agreements and provisions.

²¹⁵ Ch 5 pt B deals with disclosure and the form and effect of credit agreements.

²¹⁶ Ch 6 pt A deals with collection and repayment practices.

²¹⁷ Van Heerden 'Over-indebtedness and reckless credit' 11.3.3.2. International guidelines suggest that negotiations may be strengthened by the possibility of a formal procedure where informal initiatives fail, adequate legal aid and that passive creditors should not be able to hinder agreements. Furthermore, costs should not pose an obstacle to resolving financial problems through an informal route; ch 2 par 2.7. As the negotiation phase is not regulated by the Act, many of these elements do not form part of such negotiations.

- (1) If a debt counsellor makes a proposal to the Magistrate's Court in terms of section 86(8)(b), or a consumer applies to the Magistrate's Court in terms of section 86(9), the Magistrate's Court must conduct a hearing and, having regard to the proposal and information before it and the consumer's financial means prospects and obligations, may –
- (a) reject the recommendation or application as the case may be; or
 - (b) make –
 - (i) an order declaring any credit agreement to be reckless, and an order contemplated in section 83(2) or (3), if the Magistrate's Court concluded that the agreement is reckless;²¹⁸
 - (ii) an order re-arranging the consumer's obligations in any manner contemplated in section 86(7)(c)(ii); or
 - (iii) both orders contemplated in subparagraph (i) and (ii).

The section further provides that the NCR may not intervene in matters concerning this section.²¹⁹

Section 87 seemingly only caters for two instances, the one being where a debt counsellor makes a proposal after concluding that the consumer was not over-indebted, but likely to experience difficulty satisfying all obligations, and where voluntary negotiations were unsuccessful.²²⁰ The second instance is where a consumer approaches the court after the debt counsellor found the consumer not to be over-indebted and rejected the consumer's application.²²¹ However, it is evident that the section should also have provided for instances where the consumer was found to be over-indebted. That this *lacuna* was a mere oversight by the legislature was confirmed in *National Credit Regulator v Nedbank Ltd* where it was held that the section also finds application where a consumer was found to be over-indebted.²²²

Where a debt counsellor determines that a consumer is not over-indebted but recommends that the parties voluntarily consider and agree on a plan of debt re-arrangement,²²³ and the parties concerned accept the proposal, the debt counsellor must record the proposal in the form of an order and, with the consent of all

²¹⁸ See ch 5 par 5.5.

²¹⁹ S 87(2).

²²⁰ S 86(8)(b).

²²¹ S 86(9).

²²² In accordance with s 86(7)(c); *National Credit Regulator v Nedbank Ltd* (GNP) 304–305. This was confirmed by the Supreme Court of Appeal in *Nedbank Ltd v National Credit Regulator* 2011 (3) SA 581 (SCA) 597–598. The oversight was unfortunately not rectified by the Amendment Act.

²²³ The second option discussed above.

concerned, file the proposal as a consent order.²²⁴ As was also stated in the context of section 87, where the consumer and each credit provider do not accept the proposal, the debt counsellor must refer the matter to the magistrate's court with a recommendation.²²⁵ After an agreement has been reached or an order of court has been obtained, the consumer must abide by the provisions thereof by servicing the debt in accordance with the order or agreement. It is to be noted that debt counsellors are, in terms of their conditions of registration and now also by regulation,²²⁶ prohibited from receiving and distributing any payments and that this function is outsourced to payment distribution agencies accredited by the NCR.²²⁷

Section 86(10) provides that if a consumer is in default under a credit agreement that is being reviewed, the credit provider in respect of that credit agreement may give notice to terminate the review in the prescribed manner²²⁸ to the consumer, the debt counsellor and the NCR at any time at least 60 business days after the date on which the consumer applied for the debt review. Section 26(b) of the Amendment Act inserted section 86(10)(b) which provides that an application for debt review may not

²²⁴ S 86(8)(a). The consent order should be filed in terms of s 138 with the National Consumer Tribunal or a court. See also reg 3 Debt Counselling Regulations, 2012 which provides that it should be lodged in a manner and form prescribed by rule 55 of the Magistrates' Courts Rules when lodged with the court. Where the Tribunal is approached, its rules will prevail.

²²⁵ S 86(8)(b). No time limit is set. See *FirstRand Bank v Smith* unreported case nr 24208/2008 (W) par 24 where the court refers to a reasonable time which is, according to the court, not more than three months as referred to by Roestoff 2009 *Obiter* 434. Roestoff submits that although the NCA does not prescribe a time frame within which the debt counsellor should apply for a consent order or approach the court in terms of s 86(8), the answer is to be found in s 86(10); 436. This subsection indirectly prescribes a 60 business-day period. Van Heerden is of similar view; 'Over-indebtedness and reckless credit' 11.3.3.2. This approach was preferred in *Wesbank v Papier* 403. However, see *Wesbank v Martin* 2012 (3) SA 600 (WCC) 608 for a different opinion where the court held that the same period that is applicable to a s 86(9) scenario ought to apply. Nevertheless, such a referral will only be competent where the attempted voluntary re-arrangement did not end in a negotiated agreement or where there is no reasonable prospect that an agreement will be reached; see *National Credit Regulator v Nedbank Ltd* 317.

²²⁶ See the amendment of reg 11 by the national credit regulations which include affordability assessment regulations.

²²⁷ S 1 defines a payment distribution agent as
[a] person who on behalf of a consumer, that has applied for debt review in terms of this Act, distributes payment to credit providers in terms of a debt re-arrangement, court order, order of the Tribunal or an agreement.

The definition was inserted by s 1 of the Amendment Act. See also the newly inserted s 44A and reg 10A. See further the amended s 46 in relation to the registration and regulation of payment distribution agencies.

²²⁸ There are no further prescriptions other than those contained in s 86(10).

be terminated if the matter has been filed in the court or the Tribunal.²²⁹ However, an earlier remark by Roestoff is relevant in that credit providers are left without a remedy where a consumer has set a matter down for hearing, but does not have a real intention to proceed therewith.²³⁰ In this regard she suggests that the NCA²³¹

be amended to provide for the lapsing of debt review proceedings in terms of section 87 if it is not followed to its conclusion within a reasonable time period after referral to the Magistrate's Court.

Where a credit provider, subsequent to the provision of a termination notice, proceeds to enforce the agreement, the court hearing the matter may order that the debt review resume on any conditions that the court considers to be just in the circumstances.²³² Van Heerden submits that the termination effectively brings an end to the debt review process and thus also to the statutory function of the debt counsellor. She states that it is the responsibility of the consumer to request a resumption in terms of section 86(11), but that the court may in the alternative *suo motu* order resumption of the debt review.²³³ The Supreme Court of Appeal in *Collett v FirstRand Bank Ltd*²³⁴ found that the court referred to in section 86(11) is the enforcement court. Also, the subsection originally referred to the magistrates' courts and in this regard the court found that the words 'or High Court' should be read into

²²⁹ See Roestoff 2010 *Obiter* 782 and Van Heerden and Coetzee 2011 *PELJ* for the intricacies regarding the termination of debt review proceedings and resulting conflicting judgments prior to the amendment that inserted the proviso to s 86(10). See also Van Heerden and Coetzee 2011 *De Jure* for a discussion of *Wesbank Ltd v Papier* where the full bench held that once a matter has been referred to the magistrates' court for a determination, a credit provider may no longer terminate and subsequently attempt to enforce the agreement – which approach has now been endorsed by the legislature through the amendment. However, the Supreme Court of Appeal reached a contrary conclusion in *Collett v FirstRand Bank Ltd* 517 in that a debt review may still be terminated even where it has been referred to court. This judgment was obviously negated by the amendment; see the discussion of the *Collett* matter and the impact that it had below.

²³⁰ Roestoff 2010 *Obiter* 792.

²³¹ *Ibid.*

²³² A 86(11).

²³³ See in general Van Heerden 'Over-indebtedness and reckless credit' 11.3.3.4 and authorities referred to as regards a detailed discussion of s 86(11). Van Heerden, amongst others, submits that the consumer should provide the court with sufficient facts to justify the resumption. She also provides that a consumer need not wait for a credit provider to apply for summary judgment before making the request for a resumption of the debt review. She argues that the consumer can approach the court from which summons was issued immediately upon service of the summons. However, in such an instance, the court will have no information relating to the debt review and a substantive application coupled with supporting documents will therefore be necessary. Such an application has obvious cost implications for consumers.

²³⁴ 518.

the subsection. Section 86(11) was subsequently amended to specifically refer to 'court'.²³⁵

A consumer is 'rehabilitated' once the debt counsellor issues a clearance certificate.²³⁶ A clearance certificate must be issued within seven days after the consumer has²³⁷

- (a) satisfied all the obligations under every credit agreement that was subject to that debt re-arrangement order or agreement, in accordance with that order or agreement; or
- (b) demonstrated²³⁸
 - (i) financial ability to satisfy the future obligations in terms of the re-arrangement order or agreement under-
 - (aa) a mortgage agreement which secures a credit agreement for the purchase or improvement of immovable property; or
 - (bb) any other long term agreement²³⁹ as may be prescribed;
 - (ii) that there are no arrears on the re-arranged agreements contemplated in subparagraph (i); and
 - (iii) that all obligations under every credit agreement included in the re-arrangement order or agreement, other than those contemplated in subparagraph (i), have been settled in full.

Once the certificate is issued, the debt counsellor must within seven days file a copy thereof with the national credit register²⁴⁰ and all credit bureaux²⁴¹ that must expunge all adverse information relating to the debt re-arrangement order or agreement.²⁴²

There is no statutory maximum term within which the debt review must be completed as it only lapses once a clearance certificate has been issued in accordance with

²³⁵ See s 26(b) of the Amendment Act.

²³⁶ A clearance certificate is issued in accordance with s 71 that was extensively amended by s 21 of the Amendment Act. S 71 must be read together with reg 27 and form 19.

²³⁷ S 71(1). Where a debt counsellor refuses to issue the certificate or fails to do so, the consumer may apply for a review to the National Consumer Tribunal which may order the debt counsellor to issue the certificate if it is satisfied that the consumer is entitled thereto; s 71(3). The debtor's 'rehabilitation' is dependent on the level of payment to creditors, which is in conflict with international principles and guidelines; see ch 2 par 2.7.

²³⁸ S 71(2) provides that a debt counsellor must apply measures as may be prescribed for purposes of the demonstration.

²³⁹ The NCA does not define a 'long term agreement'.

²⁴⁰ There is no such register in existence.

²⁴¹ S 71(4). If this is not done, a consumer may file a copy with the NCR and lodge a complaint against the debt counsellor.

²⁴² S 71(5). Failure by a credit bureau to expunge such information constitutes an offence; s 71(7).

section 71.²⁴³ However, it seems that section 71(1)(b)²⁴⁴ attempts to temper the effects that the purposes of the NCA²⁴⁵ brought about in instances where the inclusion of especially mortgage agreements in the debt review procedure results in consumers being subject to the procedure for extremely long periods.

Section 88 of the NCA deals with the effects of debt review or a re-arrangement order or agreement. It provides that a consumer who has applied for debt review or who has alleged in court that he is over-indebted may not obtain any further credit, other than a consolidation agreement, before one of three events has occurred. These are that (i) the debt counsellor has rejected the application and the period within which the consumer can approach the court has expired without the consumer making use of the opportunity;²⁴⁶ (ii) the court determined that the consumer is not over-indebted or has rejected the debt counsellor's proposal or the consumer's application;²⁴⁷ or (iii) all obligations that were re-arranged by order of court or agreement between the consumer and credit providers are fulfilled – unless they were fulfilled by way of a consolidation agreement,²⁴⁸ in which case all obligations in terms of the consolidation agreement must be fulfilled.²⁴⁹ It is interesting to note that section 88(1) was not amended to reflect the new position relating to a clearance certificate as was discussed above. The effect of the omission is that where a clearance certificate is issued in instances where mortgage agreements have not been paid in full, the consumer will not be able to obtain further credit despite his financial record being cleared. The question of whether, in light of the unaffected provisions as contained in section 88(1), the amended section 71 has reached its objective comes to mind.

²⁴³ International principles and guidelines prescribe that a discharge should be possible and should not be in the too distant future. It is widely proposed that plans should be realistic and a period of between three and five years is favoured; ch 2 par 2.7. As the debt review procedure does not provide for a discharge of debt, the 'rehabilitation' of the consumer may in some instances only materialise after a substantial period has lapsed.

²⁴⁴ Inserted by s 21 of the Amendment Act.

²⁴⁵ As contained in s 3(c), (g) and (i) and which place emphasis on the satisfaction by the consumer of all obligations.

²⁴⁶ S 88(1)(a).

²⁴⁷ S 88(1)(b).

²⁴⁸ S 88(1)(c).

²⁴⁹ S 88(2).

Where a consumer incurs debt in contravention of section 88, chapter 4 part D of the NCA, which contains provisions relating to debt review and reckless credit, will not apply to that agreement.²⁵⁰ The consumer will therefore not be able to include such debt in a debt review application or allege that it has been recklessly granted.

In turn, a credit provider is prohibited from enforcing any right or security under a credit agreement, subject to sections 86(9) and 86(10), after receiving notice of court proceedings in relation to section 83,²⁵¹ section 85²⁵² or in terms of section 86(4)(b)(i)²⁵³ and until the consumer is in default²⁵⁴ and one of two events have occurred.²⁵⁵ The first is one of the three events which would lift the consumer's prohibition to enter into new credit agreements as set out above²⁵⁶ and the second is where a consumer defaults on an obligation in terms of an agreed re-arrangement or one ordered by a court or the Tribunal. It was held in *FirstRand Bank Ltd v Fillis*²⁵⁷ that a credit provider may not enforce a credit agreement in contravention of the prohibitions as set out above, but once the 'jurisdictional requirement' in section 88(3)(a) co-exists with one of the 'jurisdictional requirements' in section 88(3)(b) the credit provider may without more proceed with enforcement. Consequently, enforcement proceedings are competent without the need to provide a notice in terms of section 86(10) or section 129(1)(a) and without having to rescind a court order. In *FirstRand Bank v Evans*²⁵⁸ it was held that a re-arrangement order does not alter contractual obligations. Therefore, once the consumer defaults, the bar on enforcement is lifted and the credit provider is entitled to claim his original contractual remedies. In *Ferris v FirstRand Bank*²⁵⁹ the Constitutional Court confirmed that the breach of a restructuring order entitles the credit provider to enforce the agreement without notice and that it is the original credit agreement that

²⁵⁰ S 88(5).

²⁵¹ Relating to reckless credit.

²⁵² Relating to court-ordered debt relief.

²⁵³ A notification by a debt counsellor that a consumer has applied for debt review. The fact that the moratorium on debt enforcement is for all practical purposes competent on application for debt review is in line with international principles and guidelines as was referred to above; ch 2 par 2.7.

²⁵⁴ S 88(3)(a).

²⁵⁵ S 88(3)(b).

²⁵⁶ In terms of s 88(1)(a)–(c).

²⁵⁷ 2010 (6) SA 565 (ECP) 569–570.

²⁵⁸ 2011 (4) SA 597 (KZD) 610–611.

²⁵⁹ 44–45.

is enforceable. In *Jili v FirstRand Bank*²⁶⁰ the Supreme Court of Appeal confirmed that the remarks in *Ferris* were not *obiter*.²⁶¹

A last consequence of a debt review or re-arrangement order or agreement is that a credit agreement, other than a consolidation loan, entered into by a credit provider with a consumer in instances where the consumer has applied for a debt re-arrangement and where such re-arrangement still subsists, will be regarded as reckless credit. This is the case even if the circumstances set out in section 80 relating to instances of reckless credit are not applicable.²⁶²

It is clear from the above that the debt review process in terms of the NCA poses numerous procedural problems that are mainly due to its limited²⁶³ and somewhat clumsy provisions.²⁶⁴ Unlike the administration order procedure, that was meticulously drafted,²⁶⁵ the debt review procedure is found in a single section of the NCA and is seemingly ignorant of basic civil procedural matters. In this regard the issues that arose on the strength of the section 86(2) exclusion (prior to its amendment) serve as an example. Unfortunately and as will be seen below²⁶⁶ the amendment did not cure these problems. One further example, as was briefly referred to above, relates to the termination of a debt review procedure in terms of section 86(10) before the amendment of the section took effect. In this regard a number of divergent decisions were handed down on the question whether a debt review procedure could be terminated once a debt counsellor (having determined

²⁶⁰ [2015] JOL 32580 (SCA) 7. The judgment was delivered on 26 November 2014.

²⁶¹ See also *FirstRand Bank Limited v Kona* case number 20003/2014 (SCA) (13 March 2015) 8.

²⁶² Van Heerden 'Over-indebtedness and reckless credit' 11.3.3.6 submits that such a contravention creates a new category of reckless credit in addition to the three types contained in s 80. See also ch 5 par 5.5.

²⁶³ The Act itself contains no provisions detailing the procedure that should be followed to bring the matter before a court and also no procedure for the court to utilise once the matter is in court. However, some solutions have been brought about by the judgments in *National Credit Regulator v Nedbank Ltd* (GNP) and *National Credit Regulator v Nedbank Ltd* (SCA) and the Debt Counselling Regulations, 2012. Nonetheless, it should be noted that it should not be necessary to cure procedural problems by means of litigor regulations.

²⁶⁴ See Roestoff *et al* 2009 *PELJ* 247 for a detailed discussion of practical problems experienced with the debt review procedure. Although their article was written prior to the amendments it highlights the problems that arise when a procedure is not properly thought through; see also Grobler 2010 April *De Rebus* 22; see further Van Heerden 'Over-indebtedness and reckless credit' 11.6.

²⁶⁵ See in general par 4.2.

²⁶⁶ See par 4.3.3.

that a consumer was indeed over-indebted) has referred the matter to a magistrate's court for an order in terms of section 86(7)(c) and whilst the hearing in terms of section 87 was still pending.²⁶⁷ The Supreme Court of Appeal finally clarified the issue in *Collett v FirstRand Bank Ltd*, a decision that was to the detriment of debt-stricken consumers. It was held that a referral to the magistrate's court did not bar a credit provider from terminating the debt review procedure. It was thus held that the right to terminate a debt review procedure continues until the court has made a section 87 order. However, the court explained that the termination only relates to the specific credit agreement and not to the hearing itself. The court also specified that the right to terminate was balanced by the consumer's right to apply for a resumption in accordance with section 86(11). Although the court argued that 'the hearing continues and, if several credit agreements are being reviewed, continues in respect of the others',²⁶⁸ it is submitted that the termination of one or more agreements would derail the entire process. This is so as the consumer's situation as a whole is under consideration (as opposed to individual agreements) and the exclusion of a particular agreement has a domino effect on others. Fortunately the legislature came to the assistance of consumers in this regard as section 86(10) was amended by including the proviso thereto as discussed above. However, as Roestoff points out,²⁶⁹ creditors are left without a remedy where consumers do not see to it that the matter is brought to a close.

Further relating to the NCA's weak procedural provisions, according to a research report by the law clinic of the University of Pretoria²⁷⁰ in collaboration with the University's Bureau for Statistical and Survey Methodology on the reasons for the ineffectiveness of the debt review process, the vagueness and insufficiency of the NCA and its regulations were second on the list of major obstacles in the process.²⁷¹

²⁶⁷ See Van Heerden and Coetzee 2011 *PELJ* 37 for a discussion of cases decided prior to *Collett v FirstRand Bank Ltd*. See also Van Heerden and Coetzee 2011 *De Jure* 463.

²⁶⁸ 2011 (4) SA 508 (SCA) 517.

²⁶⁹ Roestoff 2010 *Obiter* 792.

²⁷⁰ University of Pretoria Law Clinic *The debt counselling process* 307. This report was commissioned by the NCR.

²⁷¹ Credit providers who fail to co-operate were first on the list; *ibid*. In a follow-up report it was found that stakeholders are still uncertain about sections of the NCA and regulations as these 'were perceived to be ambiguous, difficult to interpret and leading to contradictory judgements' notwithstanding the fact that many aspects have (seemingly) at the time been clarified by means of judicial interpretation; University of Pretoria law clinic *An assessment* 10.

Because of the uncertainty pertaining to procedural matters the NCR was compelled to lodge an application with the high court for a declaratory order in terms of section 16(1)(b)(ii).²⁷² Furthermore and as was previously referred to, Debt Counselling Regulations²⁷³ have been published to fill some of the procedural gaps and the Amendment Act has also, although rather unenthusiastically, attempted to solve some of the procedural issues. Also, *Task team agreements* have been drafted by the credit industry forum to 'address operational and process weaknesses that come with implementation of debt review provisions'.²⁷⁴

Some early observations as regards substantive matters are that, contrary to international principles and guidelines, the debt review procedure does not (directly) make provision for the realisation of excess assets to service debts. It further does not allow for any discharge of debt, including costs and interest²⁷⁵ and does not prescribe a maximum term. A curious attribute of the procedure is that secured credit agreements are included without ranking the creditors as preferent to unsecured creditors. Although the large number of opposed applications can be ascribed to this fact, Steyn notes that locking secured creditors into the procedure may provide a potential avenue for debtors to avoid execution against their homes. In fact, the Constitutional Court held that²⁷⁶

[i]f judgment debt can be satisfied in a reasonable manner, without involving those drastic consequences, (of poor consumers losing their homes) that alternative course should be judicially considered before granting execution orders.

In *FirstRand Bank Limited v Maleke*²⁷⁷ applications for default judgment and orders declaring mortgaged homes specially executable were refused and the court encouraged the debtors to apprise them of their rights in terms of the NCA as the matters were according to the court suited for the debt review procedure.

²⁷² *National Credit Regulator v Nedbank Ltd* (GNP).

²⁷³ 2012.

²⁷⁴ See www.ncr.org for the latest agreements in this regard.

²⁷⁵ Except where the credit provider did not comply with the NCA's provisions; s 86(7)(c)(ii)(dd).

²⁷⁶ See *Gundwana v Steko Development CC* 2011 (3) SA 608 (CC) 625–626. See also Steyn 2013 *Int Insolv Rev* 163–165 where she raises these issues.

²⁷⁷ 2010 (1) SA 143 (GSJ) 159–160. See also Steyn 2013 *Int Insolv Rev* 163.

Other general observations are that the NCA does not limit the number of times that a consumer may apply for debt review. It further does not provide for the expiry of a specified period before a consumer may once again apply for the debt review procedure. However, it has been held that a consumer is not entitled to delay enforcement proceedings by applying for debt review after termination but prior to enforcement.²⁷⁸

It is clear from the above that the NCR plays an important role in the debt review process. This independent statutory body,²⁷⁹ which was first established by the NCA,²⁸⁰ has jurisdiction throughout the country²⁸¹ and is only subject to the Constitution and the law.²⁸² Its functions and responsibilities include duties 'relevant to the monitoring and safeguarding of consumer rights in South Africa and the development of an accessible creditor market'.²⁸³ It is, amongst others, specifically tasked with the registration and regulation of credit providers, credit bureaux, debt counsellors and payment distribution agencies and has to ensure that the NCA's provisions are enforced.²⁸⁴ In the fulfilment of its functions and according to section 12(4)(a), the NCR 'may have regard to international developments in the field of consumer credit'.

4.3.3 Access requirements, exclusions and the effect thereof

From the discussion of the application of the NCA²⁸⁵ it is clear that the debt review procedure is only concerned with credit agreements entered into by natural persons as consumers. Debts that do not qualify as credit agreements will therefore be excluded from the debt review procedure. These may include delictual (tort) claims, clothing accounts, professional services and municipal accounts where no interest is charged. However, some credit agreements entered into by natural persons as consumers may be excluded from the debt review procedure where the NCA limits the protection afforded to the consumer under such an agreement, for instance a

²⁷⁸ *Changing Tides 17 (Pty) Ltd v Grobler* [2012] 3 All SA 518 (GNP) 524–825.

²⁷⁹ S 12(1)(c).

²⁸⁰ S 12.

²⁸¹ S 12(1)(a).

²⁸² S 12(1)(c).

²⁸³ Scholtz 'Consumer credit institutions' 3.2.

²⁸⁴ See in general ch 2 pt A of the NCA.

²⁸⁵ Par 4.3.1.

credit guarantee where the principal agreement does not fall within the ambit of the NCA. Furthermore, where a credit provider has proceeded to take steps to enforce the agreement, such agreement cannot be included in the process.²⁸⁶ In this regard, the Supreme Court of Appeal in *Nedbank v National Credit Regulator*,²⁸⁷ which was decided before the amendment to section 86(2) had taken effect,²⁸⁸ held that the provisions of section 86(2) barred a consumer from including a specific agreement in the debt review procedure as soon as a section 129(1)(a) notice²⁸⁹ has been delivered²⁹⁰ in respect of that credit agreement.²⁹¹ Section 86(2) now provides that

²⁸⁶ S 86(2).

²⁸⁷ 590. See Van Heerden 'Over-indebtedness and reckless credit' 11.3.3.2 for a detailed discussion of case law prior to this decision.

²⁸⁸ See s 26(a) of the Amendment Act.

²⁸⁹ The s 129(1)(a) notice is a letter which a credit provider must send to a defaulting consumer before such credit provider may commence legal proceedings to enforce the agreement. This notice, amongst others, serves to inform the consumer of his right to consult a debt counsellor. The purpose of the notice is for parties to resolve any dispute under their agreement or to develop and agree on a plan to bring payments up to date.

²⁹⁰ A question that gave rise to much confusion, due to conflicting judgments, was whether the notice is effective and constitutes compliance with the NCA only once the consumer has received same. In *Rossouw v First Rand Bank Ltd* 2010 (6) SA 439 (SCA) 450 the Supreme Court of Appeal held that the despatch of the notice in the manner as chosen by the consumer constitutes compliance. It was also held that the consumer carries the risk of non-receipt as it is the consumer who elected the manner of delivery. However, the Constitutional Court in *Sebola v Standard Bank of South Africa Ltd* 168 came to a different conclusion. The court held that a credit provider who wishes to enforce the agreement must prove that the notice was delivered to the consumer. In unopposed matters, where the credit provider posted the notice, proof of the registered despatch to the address of the consumer coupled with proof that the notice reached the correct post office would constitute delivery. However, where a consumer alleges that the notice did not reach him, the court must investigate the truth of the allegation. If the court finds that the notice did not reach the consumer the court must in accordance with s 130(4)(b) adjourn the matter and set out the steps that the credit provider must take before the matter may be resumed. This decision led to legal uncertainty, the main point of contention being whether *Sebola* allows a consumer to unreasonably fail to collect or attend to properly dispatched notices – thereby prohibiting credit providers to enforce their rights under credit agreements; see for instance *Nedbank Ltd v Binneman* 2012 (5) SA 569 (WCC) and *ABSA Bank Ltd v Mkhize* 2012 (5) SA 574 (KZD). For a discussion of the mentioned cases see Van Heerden and Coetzee 2012 *Litnet* 254. See also *Balkind v ABSA Bank* 2013 (2) SA 486 (ECG) 486. However, the Constitutional Court in *Kubyana v Standard Bank of South Africa Ltd* 2014 (3) SA 56 (CC) 70–72 and 75–76 held that the wording of the *Sebola* judgment was unnecessarily broad and that it is misstated in law to imply that a credit provider will not have discharged its obligations in terms of s 129 where a consumer acts unreasonably in not collecting or attending to properly dispatched notices. S 129 was subsequently amended by s 32 of the Amendment Act by, amongst others, adding subsections (5), (6) and (7) which provide as follows:

(5) The notice contemplated in subsection (1)(a) must be delivered to the consumer
(a) by registered mail; or
(b) to an adult person at the location designated by the consumer.

(6) The consumer must in writing indicate the preferred manner of delivery contemplated in subsection (5).

(7) Proof of delivery contemplated in subsection (5) is satisfied by –

(a) written confirmation by the postal service or its authorised agent, of delivery to the relevant post office or postal agency; or

(b) the signature or identifying mark of the recipient contemplated in subsection (5)(b).

[a]n application in terms of this section may not be made in respect of, and does not apply to, a particular credit agreement if, at the time of that application, the credit provider under that credit agreement has proceeded to take the steps contemplated in section 130 to enforce²⁹² that agreement.

It is clear that a credit provider's compliance with section 129 will no longer bar the inclusion of the agreement in terms of which the notice was despatched in a debt review procedure. However, the debate as to the exact point in time at which a consumer will be barred from doing so has once again been opened, and more specifically, whether that moment is the issuing or the service of a summons. It is submitted that it ought to be the latter.²⁹³

In summary, where the majority of a consumer's debts do not qualify as credit agreements; or where some agreements have been excluded from the debt review process for instance where it qualifies as a credit guarantee, but the principal agreement is excluded; or where the consumer has already been struggling financially for some time, which caused his creditors to proceed with enforcement of such debt; or where more than one of these exclusions are present, it may not be sensible to employ the debt review procedure as a debt relief measure. Furthermore, although the debt review procedure does not specifically require that the consumer show an advantage for credit providers, it will only assist the mildly over-indebted consumer, as courts will only, in line with the purposes of the NCA that favours satisfaction of all obligations, confirm viable proposals.²⁹⁴ This is evident from the judgment of the Supreme Court of Appeal in *Seyffert v FirstRand Bank*²⁹⁵ where it was held that:²⁹⁶

²⁹¹ Most commentators did not agree with the court's interpretation that the delivery of a s 129(1)(a) notice excluded an agreement from the debt review procedure. However, commentators were not in agreement as to the moment at which such an agreement would be excluded, and more particularly whether it would be the issuing or the service of a summons; see Boraine and Renke 2008 *De Jure* 9 n186; Van Loggerenberg *et al* 2008 January/February *De Rebus* 40; Roestoff *et al* 2009 *PELJ* 260–261 and Coetzee *Impact* 86–87.

²⁹² Compulsory sequestration proceedings are not regarded as enforcement proceedings; *Investec Bank Ltd v Mutemeri* 2010 (1) SA 265 (GSJ) 274; *Naidoo v ABSA Bank Ltd* 2010 (4) SA 597 (SCA) 600–601 and *FirstRand Bank Limited v Kona* 6–7.

²⁹³ Coetzee *Impact* 86–87.

²⁹⁴ Johnson and Meyerman *Insolvency systems* 20 and Roestoff and Coetzee 2012 *SA Merc LJ* 16.

²⁹⁵ See also *Collett v FirstRand Bank Ltd* 517.

²⁹⁶ *Seyffert v FirstRand Bank* 586.

Their [the consumers'] restructuring proposals were simply, as the court below found, 'devoid of economic rationality', and would have left a substantial part of the debt unpaid.

The court found that:²⁹⁷

[T]he appellants' proposals ... will not lead to the discharge of their debt ... and their evidence falls short of inspiring confidence that their affairs would improve so as to enable them to eventually discharge their obligations. Neither of the proposals envisages the discharge of the debt within the agreed period or within any suggested, and feasible, extended time. This is not a case where a debt review can usefully be employed.

As all three statutory debt relief measures have now been considered, it is evident that a consumer who does not qualify for the sequestration procedure (due to the 'advantage requirement') and also does not qualify for the administration procedure (where the majority of the debt are for instance *in futuro* debt or where the total amount of debt is more than R50 000) may further be excluded from utilising the debt review procedure due to the factors considered in this paragraph.²⁹⁸ A significant number of debtors who are excluded from any and all statutory measures fall into the NINA category. This is because 'asset less' insolvents will not qualify for the sequestration procedure and 'income less' consumers will not qualify for one of the statutory repayment plans, namely, the administration order and debt review procedures.²⁹⁹

4.3.4 Effect of the sequestration and administration order procedures on the debt review procedure

In chapter 3 the impact of the administration order and debt review procedures on sequestration proceedings was considered.³⁰⁰ The effect of sequestration proceedings on the administration order procedure was investigated in paragraph 4.2.5. The issues that remain to be addressed for purpose of this discussion are the impact of the sequestration procedure on the debt review procedure and the impact of the two secondary statutory debt relief measures on each other.

²⁹⁷ *Idem* 587.

²⁹⁸ See also Boraine and Roestoff 2014 *THRHR* 374.

²⁹⁹ The exclusion of a group of debtors from any form of recourse conflicts with international principles and guidelines; ch 2 par 2.7.

³⁰⁰ See ch 3 par 3.3.2.3.

Although the interplay between the debt review procedure and sequestration proceedings is, save for one issue,³⁰¹ not addressed by the NCA or the Insolvency Act, the court in *Ex parte Ford* held that it may exercise its discretion to determine the most appropriate mechanism in relation to the facts before it. A court may thus deny a voluntary surrender application on the basis that the NCA may provide a more appropriate remedy.³⁰² The other side of the coin, namely, the impact of sequestration procedures on the procedures relating to debt review in the NCA is also investigated. In this regard the decision in *Investec Bank Ltd v Mutemeri*³⁰³ stands out. In this matter the applicants applied for the compulsory sequestration of the respondents who were deemed to be married in community of property. The respondents' most prominent defence was that the NCA barred the application for their sequestration. They argued that that was the case as they had applied to a debt counsellor for a debt review in terms of section 86 of the NCA and that the matter had already been referred to court for a restructuring order by the time that the application for their compulsory sequestration was initiated. The respondents submitted that until the hearing relating to the debt review had taken place, no legal proceedings for enforcement of claims could be instituted against them and that an application for compulsory sequestration amounted to such proceedings.³⁰⁴ The respondents relied on sections 129(1) and 130(1) and the question that the court had to decide was whether the application for compulsory sequestration was an application to enforce a credit agreement within the meaning of section 130(1).³⁰⁵

The court stated that there is little doubt that a creditor's motive in applying for compulsory sequestration may be the payment of debt. It considered a number of cases that dealt with the nature of compulsory sequestration proceedings, starting with a reference³⁰⁶ to the judgment of the appellate division in *Estate Logie v Priest*³⁰⁷ where Solomon remarked that

[i]t appears to me that it is perfectly legitimate for a creditor to take insolvency proceedings against a debtor for the purpose of obtaining payment of his debt.

³⁰¹ See the schedule to the Amendment Act and the newly inserted s 8A of the Insolvency Act.

³⁰² *Ex parte Ford* 383–384; See the discussion of the case in ch 3 par 3.3.2.3.

³⁰³ See Boraine and Van Heerden 2010 *PELJ* 98 *et seq* for a discussion of the case.

³⁰⁴ *Investec Bank Ltd v Mutemeri* 268.

³⁰⁵ *Idem* 274.

³⁰⁶ *Ibid.*

³⁰⁷ 1926 AD 312 319.

In truth that is the motive by which persons, as a rule, are actuated in claiming sequestration orders. They are not influenced by altruistic considerations or regard for the benefit of other creditors, who are able to look after themselves. What they want is payment of their debt, or as much of it as they can get.

However, according to the court, the question whether an application for sequestration constitutes an application 'for an order to enforce a credit agreement' as intended in section 130(1), depends on the nature of the relief that the creditor seeks and not on his motive in bringing the application.³⁰⁸

The court referred to another decision by the then appellate division, *Collett v Priest*,³⁰⁹ where the court had to consider whether a sequestration order made by a specific court could be taken on appeal to another. The statute under consideration permitted appeals in 'any civil suit'. The court held that a 'civil suit' was a legal process where one party sues or claims something from the other and that it did not include an application for sequestration. The court in *Mutemeri*³¹⁰ quoted an explanation from the court in *Collett v Priest* where it was held that:

The order placing a person's estate under sequestration cannot fittingly be described as an order for a debt due by the debtor to the creditor. Sequestration proceedings are instituted by a creditor against a debtor not for the purpose of claiming something from the latter, but for the purpose of setting the machinery of the law in motion to have the debtor declared insolvent. No order in the nature of a declaration of rights or of giving or doing something is given against the debtor. The order sequestering his estate affects the civil status of the debtor and results in vesting his estate in the Master. No doubt before an order so serious in its consequences to the debtor is given the court satisfies itself as to the correctness of the allegations in the petition. It may for example have to determine whether the debtor owes the money as alleged in the petition. But while the court has to determine whether the allegations are correct, there is no claim by the creditor against the debtor to pay him what is due nor is the court asked to give any judgment, decree or order against the debtor upon any such claim.

Trengrove J also referred to *Prudential Shippers SA Ltd v Tempest Clothing Co (Pty) Ltd*³¹¹ which involved an application for the winding-up of an estate. The respondent alleged that the debt had arisen from a moneylending transaction subject to a specific piece of legislation and asked that the applicant's officers be examined

³⁰⁸ *Investec Bank Ltd v Mutemeri* 274. It is interesting to note that some courts do take the motive of an applicant creditor into account; see the discussion of friendly applications in ch 3 par 3.3.2.2.

³⁰⁹ 1931 AD 290 299.

³¹⁰ *Investec Bank Ltd v Mutemeri* 275.

³¹¹ 1976 (2) SA 856 (W).

under a particular section in the Act which provided for such an examination in any proceedings ‘for the recovery of a debt’ in pursuance of a money lending transaction. However, it was held that an application for the winding-up of an estate is not proceedings ‘for the recovery of a debt’.³¹²

Trengrove J found that the same rationale as that employed in the above mentioned judgments was applicable to the question under consideration in the *Mutemeri* case. The court found that section 130(1) only applies to an application for an order to enforce a credit agreement which does not include an application for compulsory sequestration as it is not concerned with enforcement. The court also referred to section 9(2) of the Insolvency Act which provides that a sequestrating creditor’s claim need not be due, thus need not be enforceable as yet. The court consequently confirmed that the purpose and effect of an application for sequestration are to bring about a convergence of the claims in an insolvent estate to ensure that the estate is wound up in an orderly fashion and that creditors are treated equally.³¹³ The requirement that an applicant must have a liquidated claim is not because the application is for the enforcement of the claim, but merely to ensure sufficient interest in the matter. Once the order is granted, the enforcement of the applicant’s claim is subject to the same rules that apply to claims of other creditors of the estate. The court therefore held that, as an order for sequestration is not an order for enforcement, it is not subject to section 130(1).³¹⁴ The respondents also relied on section 88(3). The section provides that a credit provider who received a notice regarding the consumer’s application for debt review ‘may not exercise or enforce by litigation or other judicial process any right or security’. However, as it was held that an application for compulsory sequestration does not amount to the exercise or enforcement of a right, section 88(3) was not applicable to such proceedings.³¹⁵

Boraine and Van Heerden agree with the decision that an application for compulsory sequestration does not constitute enforcement proceedings. In addition to the arguments of the court in *Mutemeri*, they submit that an application for compulsory

³¹² *Investec Bank v Ltd Mutemeri* 275.

³¹³ See also ch 3 par 3.3.1.

³¹⁴ *Investec Bank Ltd v Mutemeri* 275–276.

³¹⁵ *Ibid.*

sequestration does not result in a civil judgment that turns the credit provider into a judgment creditor. Further arguments are that the nature and purpose of sequestration as opposed to debt enforcement are that the insolvent estate vests in the trustee, which prevents the debtor from disposing of such property; that the trustee may hold enquiries to search for property disposed of; and that the trustee has extensive powers to trace estate property. They also refer to the fact that a sequestration order brings about a *concursum creditorum*. The commentators recognise that insolvency proceedings may be viewed as a collective debt-collecting device, but highlight the differences in collective *versus* individual debt enforcement. Further, they note that part C of chapter 6 of the NCA is headed ‘Debt enforcement by judgment and repossession’ – thus strengthening the argument that debt enforcement in terms of the NCA must be interpreted restrictively.³¹⁶

Nonetheless, Boraine and Van Heerden are of the view that a pending debt review does have an effect on compulsory sequestration applications and specifically on the ‘advantage for creditors’ requirement’. They note that the dynamics of a compulsory sequestration application differs remarkably from that of a voluntary sequestration application, most importantly as the sequestrating creditor will generally not have intimate knowledge of the debtor’s financial affairs. It is also for this reason that he carries a lighter onus.³¹⁷ The writers consequently submit that it would be unreasonable for a court to require the applicant-creditor to address it on the advantages of debt rearrangement or restructuring in terms of the NCA as opposed to sequestration proceedings. However, it will be possible for the debtor or a creditor to intervene and oppose an application for compulsory sequestration on the basis that the debt review procedure may be more advantageous to creditors. In this regard an intervening party should be ‘armed with facts’ supporting their contentions as mere speculation will not suffice. Boraine and Van Heerden therefore reach the conclusion that a court should not reject an application for sequestration on ‘a vague notion that debt review is the more suitable remedy’ and that the court must apply its mind judicially within the realm of the advantage requirement.³¹⁸ In this regard the court holds an ultimate discretion in deciding whether sequestration will be the best

³¹⁶ Boraine and Van Heerden 2010 *PELJ* 109–111.

³¹⁷ See ch 3 par 3.3.2.1.

³¹⁸ Boraine and Van Heerden 2010 *PELJ* 114–115.

solution under the circumstances when contemplating the advantage requirement.³¹⁹ The authors finally caution that debt review should not be turned into an added statutory requirement for the reasons mentioned above and that such an addition will increase expenses. They state that, at best, debt review should remain a factor when exercising the court's discretion.³²⁰ Boraine and Van Heerden is thus of the opinion that the estate of a debtor under debt review may be sequestrated.³²¹

In *Naidoo* the Supreme Court of Appeal confirmed the soundness of *Mutemeri* in that sequestration proceedings do not amount to enforcement proceedings as contemplated in the NCA.³²² Although Maghembe submits that the reasoning in *Naidoo* is sound he expresses concern regarding the effect of the decision on the efficiency of the NCA in that it does not provide a consumer with an option to continue with debt review proceedings when sequestrated.³²³ He points out that the NCA provides that one of the methods of fulfilling the aims thereof is the principle of satisfaction of all financial obligations,³²⁴ which is contrary to the effect that a sequestration order will undoubtedly have. He also states that a debtor should not be forced to be subjected to the social stigma of insolvency without being given a choice between insolvency and other debt relief measures.³²⁵ Such a choice will have the added benefit of enabling the consumer to keep his assets which is also one of the purposes of the NCA.³²⁶ Maghembe reasons that *Naidoo* is inconsistent with this goal and therefore opines as follows:³²⁷

³¹⁹ See also Van Heerden and Boraine 2009 *PELJ* 44–46 for a discussion of the court's discretion in insolvency applications and the advantage requirement.

³²⁰ Boraine and Van Heerden 2010 *PELJ* 115.

³²¹ *Idem* 117.

³²² 600–601.

³²³ Africa 2012 *Obiter* 410 questions the soundness of the judgment and states that by simply giving the words 'any proceedings' in section 130(3)(a) its ordinary meaning, it seems that the legislature intended that the National Credit Act should apply to all proceedings commenced in a court of which credit agreements are the cause. It is submitted that sequestration proceedings, notwithstanding the fact that it does not qualify as debt enforcement proceedings, should fall within the ambit of 'any proceedings' as meant by section 130(3)(a) of the National Credit Act.

See 410–411 as regards further reasons for the submission.

³²⁴ He refers to s 3(g).

³²⁵ International guidelines are not in agreement as to whether the choice of accessing a particular procedure should be left with the debtor or a disinterested third party. The *WB Report* favours the position where disinterested third parties are left with such decisions; ch 2 par 2.7.

³²⁶ Maghembe 2011 *PELJ* 176–178.

³²⁷ *Idem* 178.

As a result of this decision, any potential that the consumer may have to fulfil his or her financial responsibility and avoid becoming insolvent may be side-stepped by a credit provider who applies for sequestration directly.

Maghembe submits that the same holds true for the problem created by section 88(3) and that once a debt restructuring has been granted a credit provider should not be allowed to proceed with sequestration proceedings against the debtor as this is inconsistent with the principle of encouraging consumers to pay off their debt. He is accordingly of the opinion that the NCA should be amended to preclude creditors from applying for compulsory sequestration after they have received a notice that the consumer has applied for debt review or that the matter has been referred to a court for debt review.³²⁸

In line with the above reasoning, Steyn submits that the fact that a mortgagee may bring a compulsory sequestration application after an application for debt review leaves the homeowner debtor in a vulnerable position. This also undermines the efficacy of the NCA as a consumer debt relief measure and its capacity to protect a debtor from the forced sale of his home. As mortgagees are prohibited from individual enforcement proceedings whilst the mortgage agreement is subject to debt review, but not from instituting compulsory sequestration proceedings, it may tend towards abuse of the sequestration process.³²⁹

It is questionable and unfortunate that, despite the above submissions by commentators, the Amendment Act did not address this matter at all.

A further question that was raised within the context of the interplay between the debt review and sequestration procedures is whether an application for debt review, or acts committed thereafter, would result in an act of insolvency in terms of section 8 of the Insolvency Act.³³⁰ This question gave rise to a number of diverging

³²⁸ *Idem* 178–179. See also Steyn 2012 *PELJ* 216–220 who agrees with Maghembe on the need to amend the relevant provisions of the NCA to prohibit a creditor from bringing an application for sequestration in specific circumstances.

³²⁹ Steyn 2013 *Int Insolv Rev* 166. International principles and guidelines provide that where an insolvency system allows for creditor petitions, potential misuse should be guarded against. This calls for regulation; ch 2 par 2.7.

³³⁰ See ch 3 par 3.3.2.1 as regards acts of insolvency. For an extensive discussion of the issue of whether an application for debt review or acts performed subsequent thereto result in acts of

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judgments³³¹ that created uncertainty in this regard. At the time Steyn also in this regard submitted that the potential for alternative consumer debt relief in terms of the NCA could be undermined and that abuse by credit providers who may wish to circumvent the NCA's debt enforcement requirements may potentially be encouraged. She submitted that the state of affairs was indicative of the practical need for a solution to be found in order to combat or reduce creditors' opposition or resistance to debt relief in terms of the NCA. Steyn therefore supported the call for legislative intervention also in relation to the interplay between the sequestration and debt review procedures and more specifically that it should not be possible to frustrate the debt review procedure by way of sequestration proceedings.³³² Fortunately the Amendment Act inserted section 8A into the Insolvency Act³³³ which provides that '[a] debtor who has applied for a debt review must not be regarded as having committed an Act of insolvency'.

insolvency prior to the amendment to the insolvency Act by the schedule to the Amendment Act, see Steyn 2012 *PELJ* 190 and authorities cited there. See further Van Heerden 'Over-indebtedness and reckless credit' 11.7 and Chokuda 2013 *SALJ* 5.

³³¹ See, amongst others, the following judgements: In *Nedbank Ltd v Maxwell* unreported case nr 18027/2010 (SGJ) para 11 and 12, as referred to by Van Heerden 'Over-indebtedness and reckless credit' 11.7, the court held that an application for debt review does not constitute an act of insolvency in terms of s 8(g) as the application is an indication of the intention to pay. Furthermore, as long as the respondent meets his obligations in terms of the restructured obligations the debt is not due or payable and therefore the claim is not liquidated. In *Nedbank v Andrews* (240/2011) [2011] ZAECPHC it was contended that the debtor committed acts of insolvency in terms of s 8(e) and 8(g) of the Insolvency Act in lieu of his application for debt review, but the court did not entertain the matter as the allegations were withdrawn and the court consequently did not make a finding in that regard. In *FirstRand Bank Ltd v Evans* 2011 (4) SA 597 (KZD) 602–606 it was held that a notification that a debtor has applied for debt review and will in future pay this debts in accordance with a debt re-arrangement order indicates that debt will be paid other than in accordance with existing contractual obligations which amounts to an act of insolvency in terms of s 8(g). However in *FirstRand Bank Ltd v Janse Van Rensburg* [2012] 2 All SA 186 (ECP) 192–193 the court held that *Evans* is not authority for a general proposition that an application for debt review constitutes compliance with s 8(g) of the Insolvency Act. The Constitutional Court in *De Klerk v Griekwaland Wes Korporatief Bpk* 2014 (8) BCLR 922 (CC) 926–928 in dealing with an application for leave to appeal a final sequestration order, had to decide whether a debt-restructuring proposal sent to a creditor constitutes an act of insolvency in terms of section 8(g) of the Insolvency Act. The court referred to the conflicting judgments and the fact that academic opinion as regards the interaction between the two pieces of legislation under consideration is not unanimous. However, the court found that there need not be tension between the two acts and that a solution 'would need to engage with the careful interpretive project or reading two statutes alongside each other'. Nevertheless, the court did not make a finding as the applicant was factually insolvent. It also referred to the then Amendment Bill which the court seemingly thought would rectify the situation.

³³²

Steyn 2012 *PELJ* 216 and 224.

³³³

See s 38 and the schedule to the Amendment Act.

Although this amendment addresses one aspect of the interplay between the two procedures, which marks a victory for consumers, it could have done so much more. If the amendment were to provide that an application for compulsory sequestration is not competent once an application for debt review has been made, as was suggested by Maghembe and Steyn, subject to clearly defined instances which would uplift this moratorium, many more issues would have been clarified.

The only remaining matter regarding the interplay between statutory debt relief procedures relates to the interaction between the two secondary statutory measures.³³⁴ In this regard, neither the Magistrates' Courts Act nor the NCA regulates the issue. However, as magistrates' courts are creatures of statute, it would probably be up to interested parties to oppose an application for either of the procedures on the basis that the other may be more suited to the specific circumstances.

Nevertheless, what is more likely to arise is the need to 'convert' one procedure to the other. It may for instance be sensible to reassess a consumer's situation where he was placed under administration prior to the enactment of the NCA as *in futuro* debt may be taken into account in the debt review procedure. In instances where it will result in a better solution to all role-players involved, the debtor must apply for a rescission of the administration order in terms of section 74Q³³⁵ of the Magistrates' Courts Act and thereafter apply for the debt review procedure.³³⁶ However, all parties involved should be consulted prior to the rescission application and the subsequent application for debt review to prevent opposition and the enforcement of individual obligations once the rescission has been granted.

Only in the most unusual circumstances would it be competent to substitute a debt review procedure with an administration order procedure. Even though the latter may

³³⁴ Van Loggerenberg *Jones and Buckle* 491 submits that the administration order procedure should not operate in isolation or exclusively from the reckless credit provisions in the NCA. See also Raborife-Nchabeleng 2012 *De Rebus* July 38. See ch 5 par 5.5 as regards the NCA's reckless credit provisions.

³³⁵ See par 4.2.1.

³³⁶ That this is in fact happening in practice was confirmed by an attorney administrator, Ernst du Plessis, in a conversation on 27 February 2014 at the magistrate's court for the district of Pretoria.

be more beneficial in some instances, namely, where a debtor does not have a large amount of debt, but does have judgment debt that is excluded from the debt review procedure, the consumer should have considered employing the administration order procedure before approaching the court for the debt review order. However, a debt review order may be rescinded³³⁷ and the consumer may (theoretically) thereafter apply for an administration order. It would again be wise to consult with all involved prior to such applications, although previously excluded creditors (under debt review) would not be inclined to agree to an administration order.

Finally, it is submitted by Borraine *et al* that the two secondary statutory debt relief measures may be applied simultaneously and that this does occasionally happen in practice. However, the authors submit that it is not the optimal solution due to the potential difficulties of administering both procedures and the duplication of costs. They suggest that a debtor should rather consider a voluntary distribution in combination with the debt review procedure in instances where some debt is excluded from the latter.³³⁸

It is clear from the above discussion that the failure to regulate the interplay between statutory debt relief procedures results in uncertainty and unnecessary litigation. Furthermore and in line with international guidelines, it is suggested that the choice as regards the optimal procedure should be left to a disinterested party.³³⁹ If this is done, contentious matters relating to the interplay between procedures will only in exceptional circumstances arise.

4.3.5 Relief offered

As is the case with the administration order procedure, the debt review procedure does not result in a discharge of debt³⁴⁰ and no time limit on the duration of the process is prescribed.³⁴¹ Therefore, even where a consumer is fortunate enough to

³³⁷ See also NCR *Withdrawal guidelines* 4.

³³⁸ Borraine *et al* 2012 *De Jure* 267.

³³⁹ Ch 2 par 2.7.

³⁴⁰ S 87 read together with reg 27. See also Borraine and Roestoff 2014 *THRHR* 359. International principles and guidelines prescribe a discharge because one of the principal objectives of insolvency procedures for natural persons is economic rehabilitation; ch 2 par 2.7.

³⁴¹ If the process is not abandoned prior to a determination of over-indebtedness or terminated it seems that the issuing of a clearance certificate, 'rehabilitating' the consumer, will be the only

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comply with the procedure's entry requirements, the relief that it brings about amounts to nothing more than a mere rescheduling of debt sanctioned by a court. A consumer can consequently be bound to the plan for excessive periods, even in light of the amendments to section 71³⁴² – as opposed to the sequestration procedure where definite time periods are set. In this regard it has to be emphasised that although the NCA in its purposes profess the aim of 'resolving over-indebtedness',³⁴³ the debt review procedure in some instances only perpetuates consumers' already dire financial situations.³⁴⁴

4.3.6 Some comparative aspects in relation to the sequestration and administration order procedures as regard debt relief

Much of what was noted above³⁴⁵ in the context of the administration order procedure, is also applicable when the debt review procedure is compared to sequestration proceedings.³⁴⁶ The debt review procedure's positive attributes can be ascribed to the fact that it was created to assist overcommitted debtors whereas the sequestration procedure is not deemed to primarily be a debt relief measure. The debt review procedure may for instance only be invoked by the debtor himself and not by credit providers. It is also less complicated and more economical than the involved sequestration procedure, not least because the magistrates' courts are involved as opposed to the high court which is tasked with sequestration matters. It is further not necessary to bring an application to court to rehabilitate a consumer under debt review proceedings as rehabilitation takes place through the issuing of a clearance certificate by a debt counsellor. Another advantage of the debt review procedure in comparison with the sequestration procedure is that the consumer retains custody and control of his estate, business and undertakings. Although his credit record will be affected, a debt review order does not affect a debtor's personal status. Nevertheless, the major shortcoming of the procedure and a recurring theme in this chapter is that, contrary to sequestration proceedings, it does not provide for a

means of concluding the procedure; ss 86(10), 88 and 71 read together with reg 27. See also in general the NCR *Withdrawal guidelines*.

³⁴² See par 4.3.2.

³⁴³ See s 3(g).

³⁴⁴ See also Johnson and Meyerman *Insolvency systems in South Africa* 20.

³⁴⁵ See paragraph 4.2.7.

³⁴⁶ See in general ch 3 par 3.3 in relation to the sequestration procedure.

discharge of debt or a maximum term after which the procedure and its effects would come to an end.

The debt review procedure's simplistic design, in comparison to the sequestration procedure, can probably be attributed to the fact that it is not intended to be utilised in more complex situations where debtors are hopelessly overcommitted. However, because the debt review procedure includes secured credit (which effectively negates the whole idea behind security) and no monetary limits are set on the amount of credit that may be included in the procedure, it is often opposed.

When the debt review procedure is compared to the administration order procedure³⁴⁷ it has obvious advantages for the consumer. The most important ones are that there is no monetary ceiling, which means that more consumers will be able to qualify for this procedure, and that *in futuro* debt is included. Furthermore, apart from a restructuring of debt, the court may also apply the NCA's remedial measures in relation to reckless credit.³⁴⁸ The NCR further regulates the debt counselling industry and debt counsellors are not permitted to distribute instalments as this function is outsourced to (regulated) specialised payment distribution agencies. However, where the debt review procedure excludes many debts that for instance do not resort under the NCA's jurisdiction or where debt enforcement proceedings have commenced, the administration order procedure results in a more holistic approach and solution. On a procedural level the administration order procedure is much better drafted than the scant provisions relating to the debt review procedure. The latter is still in need of amendment as the legislature failed to rectify obvious procedural gaps by means of the Amendment Act, for instance at which exact point in time enforcement proceedings will exclude debt review proceedings as regards a particular credit agreement. In contrast, it is clear that, when drafting the administration order procedure, the legislature took cognisance of general civil procedure in the magistrates' courts and elsewhere. Examples are the provisions

³⁴⁷ See Borraine *et al* 2012 *De Jure* 255–268 for a detailed comparison between the administration order and debt review procedures; see also Raborife-Nchabeleng 2012 *De Rebus* July 37 and 38.

³⁴⁸ See ch 5 par 5.5. See Borraine *et al* 2012 *De Jure* 255. However, as was referred to above, Van Loggerenberg *Jones and Buckle* 491 submits that the administration order procedure should not operate so as to exclude the reckless credit provisions of the NCA.

relating to the interplay between section 65 of the Magistrates' Courts Act and the administration order procedure and the effect of sequestration proceedings on the administration order procedure. Another laudable feature is that there was an attempt to create a balance between the interests of creditors, debtors and society. This is for instance done by allowing credit providers to enforce debt in terms of mortgage bonds, whilst allowing the court to consider instalments payable in terms thereof when determining the amount that the debtor is obliged to pay to the administrator.³⁴⁹ Although the debt review procedure includes secured credit and may thereby assist home owners, Steyn submits that³⁵⁰

as illustrated by the *Seyffert* judgments and their outcome, the debt review and debt rearrangement provisions of the NCA, as applied by the courts, do not necessarily pose a reasonable or feasible alternative to execution against a debtor's mortgaged home. It is submitted that, as in overseas jurisdictions, legislative provisions ought to be made for a repayment plan in terms of which the claim of the mortgagee of the debtor's home remains unaffected.

Following an elaborate comparison of procedural aspects relating to the administration order and debt review procedures Borraine *et al* reach the following conclusion:³⁵¹

It is suggested that lawmakers should devise one single measure providing for all debt reorganisation cases. When devising this new measure, the positive and negative aspects pertaining to administration and debt review should be taken into account and it is suggested that lawmakers should build on the existing and well-established system of debt counselling which, as opposed to administration, is currently regulated by the NCR which was created by the NCA as regulatory body. The issue of distributions to creditors, which is currently one of the major concerns with regard to administration, is also well regulated, as the NCR compels debt counsellors to use PDAs accredited by the NCR to effect the necessary distributions.

In essence, I agree with the commentators' statement. However, I need to emphasise that, although the debt review measure in substance offers a better debt relief procedure (for instance as regards regulation), when it comes to procedural matters it has much to learn from the administration order procedure.

³⁴⁹ See par 4.2.1.

³⁵⁰ Steyn 2012 *De Jure* 650–651.

³⁵¹ Borraine *et al* 2012 *De Jure* 269–270.

4.4 Evaluation in terms of the right to equality

In this paragraph final remarks are made as regards the right to equality in terms of both the South African Constitution and the Equality Act in relation to the South African insolvency system.³⁵²

The constitutional test, as was set out in *Harksen v Lane*³⁵³ and which will be applied here, was discussed in chapter 1.³⁵⁴ There it was established that the broader natural person insolvency system at the very least differentiates between categories of people, by, amongst others, drawing a distinction between those who have something to offer creditors, be it assets or income, and those who do not have something to offer. This is so since the 'have's' are allowed access to the system, through one of the three statutory debt relief measures, but the 'have not's' are excluded from any form of statutory recourse. On another level, it has been established in chapter 3³⁵⁵ that the advantage for creditors requirement indeed unfairly discriminates against some excluded debtors by only offering a discharge of debt to those who qualify for specifically the sequestration procedure. What has to be determined in this chapter is whether the broad system's exclusion of a group of debtors constitutes unfair discrimination and if so, whether it is justifiable.

As differentiation is apparent the next step in the enquiry is to establish whether the differentiation is based on a legitimate government purpose. As regards the Insolvency Act, it was determined that its object of regulating the sequestration process by ensuring an orderly and fair distribution of assets to the advantage of the creditors of an insolvent estate is legitimate.³⁵⁶ As regards the debt review procedure, the legislative purpose most likely to blame for the large number of debtors that do not qualify for the procedure, is the NCA's emphasis on ensuring satisfaction of all debt under all credit agreements.³⁵⁷ This is a sincere and laudable

³⁵² See ch 1 par 1.1 for the procedures against which the whole of the South African insolvency system is measured in this paragraph. Also refer to sources discussed there as they are not repeated in detail in this discussion. For a discussion of the sequestration procedure's benefit for creditors requirement within the context of the right to equality see ch 3 par 3.5.

³⁵³ 1998 (1) SA 300 (CC).

³⁵⁴ Par 1.1.

³⁵⁵ Par 3.5.

³⁵⁶ *Ibid.*

³⁵⁷ See par 4.3.2.

purpose, although it is not practically attainable in all instances. Nevertheless, in principle I accept the legitimacy of such purpose. As far as the administration order procedure is concerned, it is not clear why only those with disposable income are fortunate enough to qualify for the remedy and therefore its legitimacy is suspect.³⁵⁸ Viewed holistically, the legitimacy of only allowing those with the necessary means to use one of the statutory debt relief procedures is questioned. If all natural person debtors face the same financial predicament, namely insolvency, it is not clear why it would be legitimate to attach significance to the question of whether a particular debtor has sufficient means to 'buy' access. It is therefore probable that the marginalisation of a group of debtors by the insolvency system as a whole is in conflict with section 9(1) of the Constitution. Nevertheless, as was held in *Harksen v Lane*, even if the differentiation bears a rational connection to a legitimate government purpose, it may still amount to discrimination. However, before turning to the second step in the analysis, I want to emphasise that my argument is not that any specific legislative purpose is necessarily (and under all circumstances) illegitimate. The argument is rather that the existing individual statutory debt relief measures cumulatively result in systemic discrimination and is therefore illegitimate in the present context. If proper, tailor-made mechanisms existed for every debt situation and every measure led to the same end result, namely, a discharge of debt, it will probably be acceptable to provide that only a certain group qualifies for a specific procedure in accordance with the purpose that the individual procedure strives to achieve.

The second step in the test is to determine whether differentiation amounts to unfair discrimination, which was defined in *Prinsloo v Van der Linde* as meaning 'treating persons differently in a way which impairs their fundamental dignity as human beings, who are inherently equal in dignity'.³⁵⁹ As far as discrimination is concerned, the evident socio-economic difficulties already riddling the lower section of the South African economy are associated attributes and characteristics with the potential to impair the human dignity of especially NINA debtors. These debtors are affected adversely and seriously as opposed to those who have more and are thus allowed

³⁵⁸ See par 4.2 in general.

³⁵⁹ *Prinsloo v Van der Linde* 1997 (3) SA 1012 (CC) 1026.

access to statutory debt relief measures. It is therefore safe to say that the systemic exclusion of some insolvent natural person debtors from *any* statutory debt relief measure amounts to discrimination as it adds to their already undignified financial situation by keeping them in a state of poverty. In this manner the dichotomy between the 'haves' and the 'have nots' is entrenched.³⁶⁰ The question of whether such discrimination constitutes unfair discrimination comes down to the impact thereof on the complainant and others in the specific situation. In this regard, various factors must be considered.³⁶¹ In employing these factors, the impact of the discrimination is apparent and links with the reason why the differentiation amounts to discrimination. This is so as those who do not have the option of ridding themselves of excessive debt, as opposed to their more well-to-do fellow citizens, find themselves in a lower economic position in society as the NINA group is typically formed by the indigent. The second factor relates to the nature of the provision and its purpose. Although the system is not directed at harming the complainants, the reasons for excluding some debtors from the broader system cannot be readily determined as the system has developed in a haphazard fashion with no clear direction or holistic goal. As far as 'any other relevant factors' are concerned, it is important to note that the discrimination affects the rights or interests of excluded debtors severely as they will potentially be slaves to their dire financial situation indefinitely, which clearly impairs their fundamental dignity. This inescapable financial bondage leads to further socio-economic deprivation and further entrenches the concept of the dualistic South African economy.³⁶² It can therefore be said that the impact of the current insolvency system on these excluded debtors is grave when compared to those who can access the system – especially those who are in a position to access the sequestration procedure and obtain a discharge.³⁶³

On the second level, the fact that debtors who qualify for access to a secondary measure do not have access to a discharge has been tested in chapter 3. It has been established that where a debtor does qualify for a secondary measure, but,

³⁶⁰ See Coetzee and Roestoff 2013 *Int Insolv Rev* 210.

³⁶¹ See ch 1 par 1.1.

³⁶² Coetzee and Roestoff 2013 *Int Insolv Rev* 192.

³⁶³ See ch 3 par 3.3.

because there is no discharge, the extended period of repayment is excessive it would result in unfair discrimination.³⁶⁴

The final step in the enquiry is to ascertain whether the established unfair discrimination can be justified under the limitations clause. However, as was alluded to in chapters 1³⁶⁵ and 3,³⁶⁶ it is unclear how discrimination that has been categorised as being 'unfair', as it has attributes and characteristics which may potentially impair the human dignity of people as human beings, could ever be found to have been reasonable in an open and democratic society based on human dignity, freedom and equality. When the insolvency system is viewed holistically, it is difficult to contemplate how the irrational and unfair systemic differentiation that the broader natural person insolvency law creates can be justified in terms of the limitations clause. Furthermore, the application of section 36 has not saved any of the disputed laws thus far.³⁶⁷ It can therefore be inferred that such application would also not save the unfair discrimination that the broader natural person insolvency scheme creates. Therefore, because of the lack of positive conduct by the legislator, the broader insolvency system is unconstitutional, not only as some honest but unfortunate debtors are excluded from any statutory measure, but also because, as has been established in chapter 3,³⁶⁸ some debtors may be subject to secondary procedures for unconscionable terms in comparison with those who are allowed access specifically to the sequestration procedure.

Applying the standards of the Equality Act makes it clear that discrimination does take place as the lacuna in natural person insolvency law, of not making provision for those who are excluded from statutory debt relief measures on the basis of their socio economic status, directly and indirectly withholds benefits, opportunities and advantages from excluded individuals.³⁶⁹ Within the present context, socio-economic status at least resorts under paragraph (b) of the definition of prohibited grounds as the human dignity of those who are excluded, specifically NINA debtors, is

³⁶⁴ Ch 3 par 3.5.

³⁶⁵ Par 1.1.

³⁶⁶ Par 3.5.

³⁶⁷ See ch 1 par 1.1 and authorities cited there.

³⁶⁸ Par 3.5.

³⁶⁹ In accordance with the definition of discrimination in s 1(1).

undermined. Furthermore, these debtors are adversely and seriously affected in a manner at least comparable to discrimination on a listed ground. It also perpetuates systemic disadvantage as the excluded group generally forms part of the lower tiers of the economy and is therefore already in a disadvantaged socio-economic position.³⁷⁰ Secondly, it has already been established in chapter 3³⁷¹ that some of those who do qualify for secondary debt relief measures may be discriminated against (on socio-economic grounds) as ‘assetless’ insolvents do not enjoy the privilege of a discharge. Those who qualify for secondary debt relief measures and who have sufficient income to service their debt obligations over a slightly longer period will not be able to show unfair discrimination. However, those who have some disposable income and are subject to secondary measures, but who face excessively long repayment terms (or who may in some instances be subject to such procedures indefinitely) due to low income and low employment will be able to argue discrimination along the same lines as the NINA debtors.

In view of the above discussion, I believe that at least a *prima facie* case of discrimination can be made out and that the burden of proof to establish the fairness of excluding a group of debtors from any form of recourse will therefore shift to the defendant/respondent in terms of section 13. Even though the unfairness of the discrimination will be presumed it must still be determined in terms of section 14 in disputed cases. As far as presumed unfairness is concerned, each matter requires a contextual enquiry which includes the South African social, economic and political circumstances.³⁷² In this regard, I refer to some of the factors set out in subsection (3).³⁷³ It has already been argued, in the context of the Constitution, that the exclusivity of the broader insolvency law impairs human dignity.³⁷⁴ The likely impact on the excluded groups³⁷⁵ has also been discussed above. Subsection (3)(c) is important in the present context as it refers to the position of the complainant in society and whether he or she suffers from patterns of disadvantage or belongs to a

³⁷⁰ In accordance with the definition of prohibited grounds in s 1(1). See ch 1 par 1.1.

³⁷¹ Par 3.5.

³⁷² Kok *A socio-legal analysis* 148.

³⁷³ Kok notes (*ibid*) that most of the criteria mentioned in s 14(3) stem from the decision in *Harksen v Lane*.

³⁷⁴ S 14(3)(a).

³⁷⁵ S 14(3)(b).

group that suffers therefrom. NINA debtors' circumstances make for excellent examples of persons suffering from patterns of disadvantage as these debtors are already left with no income and no assets. Their over-indebtedness only extends their financial troubles. Furthermore, if it should be argued and found that the distinctions are indirectly drawn on the basis of race, subsection (3)(c) will be even more pertinent in its application due to South Africa's history of racial discrimination. The nature and extent of the discrimination can be seen as financial slavery which in some cases may endure indefinitely.³⁷⁶ The discrimination is also systemic in nature³⁷⁷ as it is not one measure on its own, but the larger system that fails the excluded group. Whether the discrimination has a legitimate purpose³⁷⁸ within the present system is doubtful as was discussed in the context of the constitutional provisions. Therefore, if one is of the opinion that the discrimination resulting from a specific procedure achieves a legitimate purpose, for instance that sequestration is an expensive procedure to follow and that it should consequently only be available where it would render some benefit to creditors, there are definitely less restrictive and less disadvantageous means to achieve the same purpose.³⁷⁹ Such means can be devised by introducing alternative debt relief measures tailored to the excluded group's needs and by providing a discharge under such measures. Finally, it appears that the legislature has not taken concrete steps to address the disadvantage which arises from or is related to the exclusion of the marginalised groups or to accommodate diversity.³⁸⁰ Therefore the fact that South African natural person insolvency law excludes some natural person debtors from its remedial measures is in conflict with the provisions of the Equality Act.

As the legislature apparently does not view the exclusion of the majority of over-indebted insolvents as a priority a test case could be prepared by non-governmental organisations specialising in poverty and/or constitutional law as its outcome could result in a temporary solution. A typical NINA debtor's plight would best illustrate the unjustifiable and unconscionable unfair systemic discrimination that the current natural person insolvency system brings about. In terms of section 172 of the

³⁷⁶ S 14(3)(d).

³⁷⁷ S 14(3)(e).

³⁷⁸ S 14(3)(f).

³⁷⁹ S 14(3)(h).

³⁸⁰ S 14(3)(i).

Constitution, only the high court, Supreme Court of Appeal or Constitutional Court may declare legislation unconstitutional and therefore such a challenge has to be brought on constitutional grounds and to the high court as a court of first instance.³⁸¹ Although the unconstitutionality of the legislative scheme may possibly be avoided by using corrective interpretation during the constitutional review, in this regard the severance method,³⁸² it will not result in an ideal long-term solution as the whole system (encompassing all statutory debt relief procedures) is in need of a serious reconsideration. However, after the legislature has been directed to rectify the situation and before actual legislative reform has taken place it is suggested that the severance technique could be considered as a possible *interim* solution. Although it is not ideal to administer NINA estates in terms of the sequestration procedure and although it will run counter to the original purpose of the legislation,³⁸³ it is the only procedure that is suited to a constitutional modification to (in the interim) accommodate NINA debtors. If this corrective measure is not applied as an interim solution, the legislation which runs counter to the objective that the proposed constitutional review seeks to achieve – namely, to increase access as opposed to decrease same – can no longer be applied. It is suggested that, in the interim, the ‘advantage for creditors’ requirement could be severed from the Insolvency Act’s access requirements. By allowing presently excluded debtors access to the system via this route, the unfair discrimination resulting from only providing a discharge in sequestration proceedings will also be circumvented. Furthermore, such an interim measure will save the debt review and administration order procedures from unconstitutionality (in the meantime) as all insolvent situations may then be administered through the sequestration procedure. In this manner, the debt review and administration order procedures could also be used for their originally intended

³⁸¹ See Albertyn *et al Introduction* 31.

³⁸² In this regard see Botha *Statutory interpretation* 195–197 in general and 197 specifically where the concept is explained as follows:

Here the court will try to rescue a provision from the fate of unconstitutionality by ‘cutting out’ a part of the provision from the rest of the text to keep the remainder constitutional and valid.

³⁸³ The second requirement for employing the severance method is that what remains of the legislation must be able to give effect to the legislative purpose. This will not be possible in the present case, as the purpose (although not directly stated) is to benefit creditors. However, severance seems to be the only plausible solution. The first requirement is that the separation of the unconstitutional part of the provision from the rest must be possible. In the present case it is and the legislation must be interpreted in light of the severance that has occurred; *ibid.*

purpose, namely, to assist debtors through periods of (temporary) financial misfortune.

4.5 Conclusion

It has been determined in chapter 3 that most natural person insolvents do not qualify for the sequestration procedure in terms of the Insolvency Act due to mostly the advantage for creditors requirement which has been found to serve an important government purpose.³⁸⁴ Still, it has been found that the procedure can only be saved from unconstitutionality if proper alternative measures are available to debtors who are excluded from its ambit.³⁸⁵ In this chapter the adequacy of secondary statutory debt relief measures for natural person insolvents, namely, the administration order procedure in terms of section 74 of the Magistrates' Courts Act and the debt review procedure in terms of section 86 of the National Credit Act, were investigated. The two measures are described as secondary as neither of the two provides for a discharge of debt, which omission and its results resonate through discussions in this chapter. Although the administration order procedure can be labelled as hybrid in nature,³⁸⁶ both secondary procedures mainly represent repayment plans and are therefore dependent on disposable income.³⁸⁷ From the outset, it is thus recognised that neither provides any form of recourse for the NINA category of debtors.

As regards the administration order procedure, the following was established in the general overview thereof. The procedure, which was introduced under English influence, represents a modified form of insolvency and is intended for the protection of debtors with small estates that generally represent the poor who are also either illiterate or ignorant about the law or both. However, it does take cognisance of creditors' interests as a secondary purpose and the Supreme Court of Appeal has held that it was enacted in the public interest.³⁸⁸ In this regard it is on par with international guidelines that profess that a balance should be struck between the interests of the debtor, creditors and society.³⁸⁹ Debtors as opposed to creditors may

³⁸⁴ See par 3.3.

³⁸⁵ See ch 3 par 3.5.

³⁸⁶ Par 4.2.1.

³⁸⁷ Para 4.2.2 and 4.3.3.

³⁸⁸ *Bafana Finance Mabopane v Makwakwa* 587–588.

³⁸⁹ Ch 2 par 2.7.

apply for the order, which renders it unnecessary to regulate the creditor abuse that is cautioned against by international principles and guidelines.³⁹⁰ However, courts may force it upon debtors for their own good. The procedure basically provides a statutory rescheduling of debt sanctioned by a court order and is economical and uncomplicated. Nevertheless, contrary to international principles and guidelines the procedure does not provide for a discharge; is heavily reliant on the magistrates' courts; allows for creditor participation as a matter of course although qualifying estates do not represent significant value; provides that the moratorium on debt enforcement only takes effect once the administration order is granted; and does not prescribe standards as regards living expenses, although the appropriate level of sacrifice in exchange for relief is inherently political.³⁹¹ While the procedure mostly takes the form of a repayment plan, it is factually hybrid in nature. However, as assets are generally not subject to realisation and distribution, the procedure accords with internationally regarded principles proclaiming that assets are usually more valuable to the debtor than what their economic value represents.³⁹² Such sentiment is especially true within the context of the administration order procedure as the Supreme Court of Appeal has established that it is generally used by the poor.³⁹³ If circumstances allow, instalments relating to a mortgage bond could be taken into account when the amount that the debtor has to pay to the administrator is set – an excellent feature which is in line with international guidelines,³⁹⁴ although its potential will only be realised if the monetary entry threshold is increased.³⁹⁵ Other features in harmony with international principles and guidelines are that secured creditors' rights are protected; the liquidity test is used as an entry requirement; existing maintenance orders are taken into account when the amount that has to be paid to the administrator for distribution is determined; and provision is made that proceedings may be re-opened and that the court may on good cause shown suspend, amend or rescind the order.³⁹⁶ The debtor is rehabilitated when the administrator issues a certificate to that effect. However, in contrast with international principles and

³⁹⁰ *Ibid.*

³⁹¹ *Ibid.*

³⁹² *Ibid.*

³⁹³ *Bafana Finance Mabopane v Makwakwa* 587–588.

³⁹⁴ Ch 2 par 2.7.

³⁹⁵ *Ibid.*

³⁹⁶ *Ibid.*

guidelines,³⁹⁷ such certificate may only be issued once the costs of administration and creditors have been paid in full.³⁹⁸

Relating to access to and exclusions from the administration order procedure, many debtors are prohibited from entrance and where debtors do qualify some debts do not form part of the process. The ill-fated entry requirement, that all debts due should not exceed the limited threshold of R50 000, evidently exclude many insolvent debtors from the procedure's purview. Debtors who cannot show an advantage to creditors and whose debts amount to more than R50 000 will thus be excluded from both the sequestration procedure and the administration order procedure. Although the threshold did not keep up with inflation, it is agreed that a drastic increase will probably render the measure's uncomplicated procedures inadequate in some instances. Another difficulty relating to access is that those who do not have income will generally not be able to apply for the administration order procedure. However, as the process clothes presiding officers with discretion, I am not entirely convinced that zero-payment plans cannot be ordered in terms of the procedure. Nevertheless, the procedure does not specifically include NINA debtors and was not devised with this category of debtor in mind and therefore, pragmatically considered, the answer to NINA debtors' plight is not found in the present administration order procedure. Another drawback as regards its application is that *in futuro* debts are excluded from the procedure which prevents a holistic solution to the debtor's financial difficulties and in many instances renders the procedure inefficient.³⁹⁹ In this regard it is agreed with Boraine that the traditional difference between secured and unsecured debts should rather be used to determine which debts should be included in and excluded from the procedure.⁴⁰⁰ Nonetheless and as was mentioned, secured creditors' substantive rights are protected, which also benefits debtors in some instances. The example of the treatment of mortgage bonds was offered as an example.⁴⁰¹

The widely publicised abuse of the administration order procedure deserves special mention. It is interesting to note that not many arguments relating to abuse by

³⁹⁷ *Ibid.*

³⁹⁸ Par 4.2.1.

³⁹⁹ Roestoff *'n Kritiese evaluasie* 431. See also par 4.2.2.

⁴⁰⁰ Boraine 2003 *De Jure* 234 and 249 and par 4.2.2.

⁴⁰¹ Par 4.2.3.

debtors have surfaced and that resentment is mostly directed at administrators. Although the Supreme Court of Appeal has clarified that administrators occupy a position of trust⁴⁰² and the procedure itself includes sanctions to bring unscrupulous administrators to book, misconduct does not frequently result in consequences. The reasons for this injustice are that debtors subject to the order are already in dire financial situations and are therefore probably not in a position to acquire legal (or other) assistance to firstly investigate whether the administrator is doing a proper job and secondly, to hold the administrator accountable (through court procedures) where it is found not to be the case. It is also not generally worthwhile for credit providers to police and intervene in individual cases in all instances. In this respect the regulation of administrators will go a long way to improve the situation.⁴⁰³

As regards the effect of sequestration proceedings on the administration order procedure, the procedural aspects are fairly well regulated. Unfortunately the choice as regards the most suited procedure is not left with a disinterested party as is seemingly the position preferred by the most recent international report, namely, that of the World Bank.⁴⁰⁴ However, it is doubtful whether the interplay is of much practical concern as estates susceptible to the administration order procedure will not generally qualify for the sequestration procedure.⁴⁰⁵

When contemplating the actual relief offered, it is apparent that the administration order procedure is seriously deficient. This is so as neither of the twin issues suggested by international principles and guidelines,⁴⁰⁶ namely, discharge and a maximum time frame is provided for. Notwithstanding the Supreme Court of Appeal's determination of the legislature's intention,⁴⁰⁷ these omissions result in debtors being subject to administration orders for extended periods. As was mentioned, Roestoff notes that the exclusion of *in futuro* debt adds to the procedure's ineffectiveness as a debt relief measure.⁴⁰⁸

⁴⁰² *African Bank v Weiner* (SCA) 368.

⁴⁰³ Par 4.2.4.

⁴⁰⁴ *WB Report* 67 and ch 2 para 2.6.2.3 and 2.7.

⁴⁰⁵ Par 4.2.5.

⁴⁰⁶ Ch 2 par 2.7.

⁴⁰⁷ *African Bank Ltd v Weiner* (SCA) 368.

⁴⁰⁸ Roestoff 'n *Kritiese evaluasie* 431. See par 4.2.6.

When the administration order procedure is compared to the sequestration procedure it poses many advantages (over the sequestration procedure) for debtors. As the administration order procedure was mainly devised for debtor protection, it does not provide for creditor petitions, negating the possibility of creditor abuse – as was mentioned and is cautioned against by international principles and guidelines.⁴⁰⁹ Furthermore, magistrates' courts are involved and therefore the application procedure is much simpler and less expensive than the sequestration procedure. Although larger and more complex estates may call for more substantial procedural regulation, it is agreed with the court in *Ex parte Van den Berg*⁴¹⁰ that more intricate procedures are not suited to estates qualifying for the administration order procedure. Other advantages over the sequestration procedure are that advantage for creditors need not be established, that it is unnecessary to approach the court for a rehabilitation order (as is the case in sequestration proceedings prior to the point in time when the automatic discharge becomes effective) and that debtors are generally allowed to retain custody and control of their estates, businesses and undertakings. However, as the administration order procedure does not result in a discharge of debt and further does not prescribe a maximum time frame, as is the case in sequestration proceedings and as was noted above, it does not provide efficient debt relief.⁴¹¹ In the latter regard the proposal made under the reform project to provide for a discharge after a period of eight years is noted,⁴¹² although the suggested period is still extremely long and contrary to international principles and guidelines that suggest a maximum period of between three and five years.⁴¹³

It is unfortunate that the South African Law Reform Commission did not consider the reform of the administration order procedure as part of the review of the law of insolvency.⁴¹⁴ Roestoff proposes that the administration order procedure should form

⁴⁰⁹ Ch 2 par 2.7.

⁴¹⁰ 817.

⁴¹¹ Par 4.2.7.

⁴¹² Par 4.2.8.

⁴¹³ Ch 2 par 2.7.

⁴¹⁴ The South African Law Reform Commission brought out its *Report on the review of the law of insolvency* in 2000. It contained a draft bill and an explanatory memorandum – hence the '2000 Insolvency Bill' and '2000 *Explanatory memorandum*' respectively. The latest versions of the documents are unofficial working copies on file with the author (hereafter 'Bill' or '2015 Insolvency Bill' and '2014 *Explanatory memorandum*' respectively). See ch 3.

part of the proposed Insolvency Act as it is an insolvency matter.⁴¹⁵ The next issue relates to the best institution to supervise the procedure. Due to the limited nature of the procedure and the estates involved, the high court is definitely not the appropriate institution or forum to facilitate the administration order procedure and consequently four options remain. Firstly, the magistrates' courts can continue with this function on the same basis as they currently do; secondly, the debtors' courts can be strengthened to provide more specialised services;⁴¹⁶ thirdly, a regulator or independent official or office can be established to deal with these matters; and finally an insolvency practitioner can be appointed to preside over such proceedings. As international principles and guidelines propose that court involvement should be reduced,⁴¹⁷ the NCR, whose functions include that it may take cognisance of international developments in the field of consumer credit⁴¹⁸ and which is already involved in the debt review procedure,⁴¹⁹ could be considered in this regard. However, its offices do not physically have a national footprint and developing countries must consider the context of existing institutions and infrastructure rather than introducing novel nationwide infrastructures that will result in significant costs.⁴²⁰ Boraine suggests that the strengthening of debtors' courts acting as specialist courts regarding debt issues will in this regard provide the ultimate solution. In the alternative, rendering the procedure subject to the supervision of a special official or a special division of the clerk of the court is proposed.⁴²¹ However, these observations were made before the NCR was established. It is submitted that the solution may lie in between the proposed institutions and therefore an investigation should be undertaken as to whether an office of the NCR could be attached to the magistrates' courts to supervise repayment plan procedures.

General observations regarding the debt review procedure included the following. It provides for debt relief through debt-reorganisation in cases of over-indebtedness

⁴¹⁵ Roestoff 2000 *De Jure* 129–130 and 135. However, she does not argue that it should be transferred *verbatim*. See also Burdette *A framework* 324–327.

⁴¹⁶ See Boraine 2003 *De Jure* 247. Although not formally created by statute, debtors' courts are formed in magistrates' courts to adjudicate on matters pertaining to s 65 and (sometimes) s 74 proceedings and also of late to hear debt review applications.

⁴¹⁷ Ch 2 par 2.7.

⁴¹⁸ S 12(4).

⁴¹⁹ See the discussion of the NCR in par 4.3.2.

⁴²⁰ WB *Report* 60–61 and ch 2 par 2.7.

⁴²¹ Boraine 2003 *De Jure* 232.

and makes specific provision for the detection and sanction of credit recklessly extended,⁴²² but contrary to international principles and guidelines⁴²³ does not provide for the realisation of excess assets to service debt. Also in conflict with international principles and guidelines,⁴²⁴ the procedure does not provide for a discharge of debt and no maximum period for which the procedure may run has been determined. The procedure may prove to be useful in instances where a significant portion of debt relates to credit agreements as regulated by the NCA and where such debts have not been excluded from the procedure.⁴²⁵ Only debtors may apply for the procedure and a moratorium on individual debt enforcement proceedings takes effect once a consumer has applied for the debt review process, which feature is in line with international principles.⁴²⁶ However, contrary to international best practice, the procedure encompasses secured credit, without ranking such claims preferent,⁴²⁷ is reliant on the magistrates' courts and consumers are solely responsible for the costs of the procedure. Although the World Bank *Report* views informal procedures with scepticism,⁴²⁸ creditors are as a matter of course consulted and negotiated with before the matter is referred to the courts. Also, as such negotiations are not specifically regulated by the NCA, many of the elements that generally strengthen such procedures⁴²⁹ do not form part of the process. The intermediaries involved, namely debt counsellors, are registered with and regulated by the NCR and specialised and regulated payment distribution agencies collect and distribute instalments. A consumer is rehabilitated once a clearance certificate is issued by a debt counsellor. However, in contrast with international principles and guidelines the issuing of such a certificate is dependent on the level of payment to creditors.⁴³⁰ The procedure does not specifically prescribe a period before which a consumer may not again apply for its relief, but it has been

⁴²² See further ch 5 par 5.5.

⁴²³ Ch 2 par 2.7.

⁴²⁴ *Ibid.*

⁴²⁵ Par 4.3.1.

⁴²⁶ Ch 2 par 2.7.

⁴²⁷ *Ibid.*

⁴²⁸ See WB *Report* 46 and ch 2 para 2.6.2.1 and 2.7. See ch 2 par 2.6.2.1. The WB generally refers to settlement procedures as informal, even where it is regulated statutorily; WB *Report* 45 *et seq.* Other sources distinguish between formal and informal procedures on the basis of statutory regulation; see Fletcher *The law of insolvency* 45 and Josling 'Alternatives to bankruptcy' 10.47 and 10.48.

⁴²⁹ Ch 2 par 2.7.

⁴³⁰ *Ibid.*

held that a consumer is not entitled to delay enforcement proceedings by applying for debt review after termination but prior to enforcement.⁴³¹ The measure does not provide for plan modification which international principles and guidelines deem to be an important aspect of repayment plans.⁴³² Unfortunately, the debt review procedure is mostly ignorant of basic civil procedural necessities and this leads to abuse.⁴³³ An example, as was noted by Roestoff,⁴³⁴ is that credit providers do not have a specific remedy where a consumer has set a debt review matter down for hearing, but is not interested in pursuing same. Also, it is unclear at which specific point in time a consumer will be barred from including a specific credit agreement in the debt review process.⁴³⁵ As regards regulation, the NCR plays an important role in registering and regulating debt counsellors and payment distribution agencies.⁴³⁶

As far as access requirements, exclusions from the debt review procedure and the effect thereof are concerned, it has been determined that the measure may not lead to a sensible solution in instances where the majority of a consumer's debt does not qualify as credit agreements and/or are excluded from the NCA or the debt review procedure. Furthermore and in accordance with the purposes of the NCA, it will only assist those mildly over-indebted consumers who can put forward viable proposals. This is supposedly so as secured credit forms part of the process without being treated preferentially.⁴³⁷

Having considered all three statutory debt relief measures for natural persons it is evident that, in contrast with international principles and guidelines,⁴³⁸ some debtors would not qualify for any of these procedures. The excluded group is mostly formed by NINA debtors and the marginalisation evidently takes place on the basis of debtors' financial means.⁴³⁹

⁴³¹ *Changing Tides 17 (Pty) Ltd v Grobler* 524–825.

⁴³² Ch 2 par 2.6.2.5 and par 4.3.2.

⁴³³ Par 4.3.2.

⁴³⁴ Roestoff 2010 *Obiter* 792.

⁴³⁵ See also par 4.3.3.

⁴³⁶ Par 4.3.2.

⁴³⁷ Par 4.3.3.

⁴³⁸ Ch 2 par 2.7.

⁴³⁹ Par 4.3.3.

An important part of the discussions considers the effect of the statutory debt relief measures on one another. As far as the effect of debt review proceedings on the sequestration procedure is concerned it has been established in chapter 3⁴⁴⁰ that although neither of the relevant pieces of legislation regulates the issue (except for one instance) a court may exercise its discretion to determine the most appropriate mechanism in relation to the facts before it and could deny a voluntary surrender application on the basis that the NCA *may* provide a more appropriate remedy.⁴⁴¹ The other side of the coin, namely, the impact of sequestration proceedings on the debt review procedure, was discussed in this chapter. In this regard the court in *Investec Bank Ltd v Mutemeri* held that an application for the debt review procedure and the subsequent referral of the matter to court do not bar an application for compulsory sequestration. The principle was confirmed by the Supreme Court of Appeal in *Naidoo*. Borraine and Van Heerden agree with the decisions, but caution that debt review should not be elevated to an additional statutory requirement as regards sequestration proceedings as it (at most) remains a factor that the courts need to consider within their discretion.⁴⁴² Another angle is pointed out by Maghembe in that the judgment in *Naidoo* may be sound, but that it could affect the efficiency of the NCA as a consumer under debt review would fulfil all financial obligations in contravention with the effect that a sequestration order will undoubtedly have. Furthermore, a debtor should not be forced to endure the social stigma of insolvency without being given a choice between debt relief measures which will have the added benefit of enabling the consumer to retain his assets. Maghembe consequently proposes legislative amendment to preclude creditors from applying for compulsory sequestration once they have received a notice that the consumer has applied for debt review or that the matter has been referred to court.⁴⁴³ Steyn supports Maghembe's proposal and adds that it may protect vulnerable homeowners.⁴⁴⁴ Unfortunately the legislature did not take note of commentators' appeals as the Amendment Act does not address this issue. In this regard the amendment of the Insolvency Act, by specifically providing that a debtor who has applied for a debt review must not be regarded as having committed an act

⁴⁴⁰ Par 3.3.2.3.

⁴⁴¹ See in general *Ex parte Ford*.

⁴⁴² Borraine and Van Heerden 2010 *PELJ* 115.

⁴⁴³ Maghembe 2011 *PELJ* 176–179.

⁴⁴⁴ See Steyn 2012 *PELJ* 216–220 and also 2013 *Int Insolv Rev* 166.

of insolvency, must be recognised. However, had the legislature, as was suggested by Maghembe and Steyn, included a provision to the effect that an application for compulsory sequestration is not competent once an application for debt review has been made, subject to clearly defined circumstances uplifting the moratorium, many more issues relating to the interplay between the two procedures would have been solved.⁴⁴⁵

When considering the interplay between the two secondary statutory debt relief measures, legislative regulation is yet again conspicuously absent. It is submitted that although magistrates' courts have limited discretion when entertaining both procedures, they are creatures of statute and therefore it would generally be up to interested parties to oppose an application for either of the procedures on the basis that the other will be more beneficial in the circumstances. Where a debtor wishes to convert from one procedure to the other, it can only be done by rescinding the existing order and thereafter applying for the other as conversion is not specifically provided for. However, such attempts may prove to be risky. Boraïne *et al* are of the view that the procedures may be applied for simultaneously but submit that debts that are excluded from the debt review procedure should rather be dealt with by supplementing the debt review procedure with voluntary agreements.⁴⁴⁶

It is submitted that many problems can be prevented by regulating the interplay between the different statutory measures by means of legislation. Furthermore, as is preferred by the World Bank *Report*, the choice as regards the most relevant procedure should rather be left with a disinterested party who can decide on the option best suited to the specific circumstances from the outset.⁴⁴⁷ Should these two suggestions be implemented, issues surrounding the interplay between procedures would only arise in exceptional circumstances.⁴⁴⁸

In relation to the actual relief that the debt review procedure offers, the same sentiments expressed in relation to the administration order procedure are

⁴⁴⁵ Par 4.3.4.

⁴⁴⁶ See Boraïne *et al* 2012 *De Jure* 267 and par 4.3.4.

⁴⁴⁷ See ch 2 par 2.7.

⁴⁴⁸ Par 4.3.4.

applicable. As was mentioned, the procedure does not offer efficient relief as it does not provide for a discharge of debt and a maximum term – despite global buy-in in this regard.⁴⁴⁹ In fact, the opposite rings true in many instances in that, despite the NCA's purpose of providing a mechanism to relieve over-indebtedness,⁴⁵⁰ it only perpetuates same.⁴⁵¹

When the different statutory debt relief measures are compared to one another, much of what was derived when the administration order procedure was compared to the sequestration order procedure is also relevant when the debt review procedure is compared thereto. The debt review procedure was created to assist over-indebted consumers, unlike the sequestration procedure that was devised for creditors' benefit. Other differences are that only debtors may apply for the debt review procedure; the procedure itself is uncomplicated and economical; rehabilitation takes place without the need to bring a court application; the consumer retains custody and control of his estate, business and undertakings; and the order does not affect the debtor's personal status. Nevertheless, the major shortcoming of the debt review procedure in relation to the sequestration procedure is that it does not provide a discharge of debt and coupled thereto does not prescribe a maximum term for which the procedure may run. Furthermore, the fact that secured credit is included without treating such claims as preferential and no monetary limits are set on the amount that may be included in the procedure, applications have been met by serious resistance from credit providers, which has certainly diluted the effectiveness of the procedure.⁴⁵²

As far as a comparison between the administration order and debt review procedures is concerned, the debt review procedure mostly provides a better option in substance due to, for instance, the lack of a monetary threshold as regards access, the fact that *in futuro* debts are included in the procedure and the regulation of the debt counselling industry by the NCR. However, the debt review procedure poses many procedural disadvantages in comparison to the administration order

⁴⁴⁹ Par 4.3.5 and ch 2 par 2.7.

⁴⁵⁰ S 3(g).

⁴⁵¹ Par 4.3.5.

⁴⁵² Par 4.3.6.

procedure. Also the administration order procedure balances the rights of debtors, creditors and society more efficiently by for instance excluding secured credit from the procedure's ambit, whilst providing that courts, in appropriate circumstances, could take instalments relating to some secured agreements into account when determining the amount that the consumer is obliged to pay to the administrator for distribution. It is agreed with *Boraine et al* that one statutory procedure as regards debt reorganisation should be devised by, amongst others, combining the positive attributes of the two procedures and that the well-established debt review system should be built upon.⁴⁵³ However, although some of the procedural elements of the administration order procedure have not been regularly used in recent times, due to for instance the threshold of R50 000 that negates its practicality in many respects, it is suggested that such provisions be revisited and seriously considered within the context of a unified repayment plan.⁴⁵⁴

Finally, and probably most importantly, this chapter has determined that there are no proper alternatives to the sequestration procedure and therefore the larger insolvency system or scheme firstly unfairly and unjustifiably discriminates against individuals who do not have access to any of the statutory procedures. Secondly, unfair and unjustifiable discrimination occurs where a debtor does qualify for access to one of the secondary statutory procedures, but where he would be subject thereto for an unconscionably lengthy period. Therefore, the fact that the broader natural person insolvency system does not provide sufficient and efficient alternative debt relief procedures to the sequestration procedure is unconstitutional.⁴⁵⁵

⁴⁵³ *Boraine et al* 2012 *De Jure* 269–270.

⁴⁵⁴ Par 4.3.6.

⁴⁵⁵ Par 4.5.

CHAPTER 5: PROPOSED AND ANCILLARY DEBT RELIEF PROCEDURES

SUMMARY

- 5.1 Introduction
 - 5.2 Proposed pre-liquidation composition
 - 5.3 The *in duplum* rules
 - 5.4 Court-ordered debt review in terms of the NCA
 - 5.5 Reckless credit in terms of the NCA
 - 5.6 Other measures in terms of the NCA
 - 5.7 Common law composition
 - 5.8 Extinctive prescription
 - 5.9 Conclusion
-

5.1 Introduction

An important development in the field of natural person insolvency law is the Law Reform Commission's suggested pre-liquidation composition as an alternative debt relief procedure.¹ This proposed debt relief measure is of great interest since it is intended to assist those insolvent debtors who are unable to prove that the surrender of their estates would benefit their creditors as a group and who are thereby excluded from utilising the sequestration procedure.² Another innovative feature is that, under certain circumstances, a discharge of debt is proposed.³ The pre-liquidation composition procedure is considered in paragraph two of this chapter to determine whether it has the potential to address the shortcomings of the broader

¹ The South African Law Reform Commission published a report titled the *Report on the review of the law of insolvency* in 2000. It contained a draft bill and an explanatory memorandum – hence the '2000 Insolvency Bill' and '2000 *Explanatory memorandum*' respectively. The latest versions of these documents are unofficial working copies on file with the author (hereafter 'Bill' or '2015 Insolvency Bill' and '2014 *Explanatory memorandum*' respectively). This research mostly refers to the 2015 Insolvency Bill except where it specifically states that the clause referred to is contained in the 2000 Insolvency Bill. See cl 118 and 2014 *Explanatory memorandum* 201 *et seq* as regards the pre-liquidation composition.

² 2014 *Explanatory memorandum* 201.

³ See cl 118(22).

natural person insolvency system⁴ which does not provide for sufficient and efficient debt relief procedures.

The remainder (and majority) of the discussions in this chapter deal with measures that have the effect of easing a natural person debtor's financial burden even though such measures cannot be categorised as mainstream debt relief procedures.⁵ While these measures are not designed with debt relief as the (primary) objective in mind, they could have the ancillary effect of providing assistance to debt-stricken natural persons and should therefore be considered in this study. Another important reason for considering these measures is that the primary⁶ and secondary⁷ debt relief procedures do not exist in a vacuum and ancillary measures have the potential to support them. However, the study does not attempt to set out and discuss all possible adjuvant legal instruments or measures that may in certain instances have the result of providing some form of debt relief to over-committed debtors. The National Credit Act's⁸ provisions relating to unlawful agreements⁹ and provisions¹⁰ are for instance not discussed here.

Paragraph three deals with the *in duplum* rules that stem from both the common law and the NCA.¹¹ These rules are discussed as they have the potential to significantly curtail the further accumulation of debt whilst the debtor is in default and most probably also under severe financial strain. The rules will generally only benefit consumers who have been in default for quite some time.

Other measures resorting under the NCA that are considered in this chapter are court-ordered debt review, reckless credit, the consumer's right to surrender goods,

⁴ Which were illustrated in chs 3 and 4.

⁵ See the discussions in chs 3 and 4 which are focused on conventional debt relief procedures for natural person debtors.

⁶ See ch 3 par 3.3.

⁷ See ch 4.

⁸ 34 of 2005 (hereafter 'the NCA').

⁹ S 89. S 89(5) sets out the consequences of unlawful agreements. See Otto 'Conclusion, alteration and termination of credit agreements' 9.3.4.1; Otto and Otto *NCA explained* 27.2; and Kelly-Louw and Stoop *Consumer credit regulation* 196–200.

¹⁰ S 90. S 90(4) sets out the consequences of unlawful provisions. See Otto 'Conclusion, alteration and termination of credit agreements' 9.3.4.2; Otto and Otto *NCA explained* 27.3; and Kelly-Louw and Stoop *Consumer credit regulation* 200–205.

¹¹ See s 103(5) as regards the latter.

cooling-off and early settlement. A discussion of court-ordered debt review is found in paragraph four. This measure is provided for in section 85 of the NCA and can be utilised as an alternative port to a court-ordered debt restructuring as was discussed in chapter 4.¹² The NCA's reckless credit provisions provide a powerful deterrent against the extension of reckless credit due to the consequences that the latter may have, especially for a creditor. However, these consequences also have the potential of providing debt relief and are therefore further explored in paragraph five.

The right to surrender goods is an instrument that can be employed by an over-committed consumer in the management of his insolvent estate. This consumer right is contained in section 127 of the NCA and provides for the unilateral termination of certain types of credit agreements by surrendering the goods that form the subject of such agreements. The right to surrender and a consumer's concomitant right to claim compensation in instances where the section 127 procedure was not properly followed, as is provided for in section 128, are considered in paragraph six. The cooling-off and early settlement rights are also discussed in this paragraph. The common law composition and specific manifestations thereof, namely, release, compromise and novation, provide an over-committed debtor with a tool to negotiate debt relief and are considered in paragraph seven. Extinctive prescription in terms of the Prescription Act¹³ which provides relief through the lapse of time is discussed in paragraph eight.

The chapter is concluded in paragraph nine.

5.2 Proposed pre-liquidation composition

The Law Reform Commission has proposed that provision be made for a pre-liquidation composition¹⁴ with creditors.¹⁵ The proposed measure is supposed to

¹² See par 4.3.

¹³ 68 of 1969.

¹⁴ The 2015 Insolvency Bill uses the term 'liquidation' when referring to both the liquidation of juristic persons and the sequestration of natural persons and partnerships. The title of the proposed provision is confusing, as it could mistakenly be interpreted to require a composition as a precondition for liquidation proceedings. The better suited title of 'statutory proposal' is suggested.

¹⁵ The commission proposed that provision be made for such composition by inserting a new section, s 74X, in the Magistrates' Courts Act 32 of 1944; 2000 *Explanatory memorandum* and Footnote continues on next page

afford debt relief to natural person debtors¹⁶ who cannot pay their debts,¹⁷ but who are unable to prove advantage for creditors and are consequently excluded from the liquidation process.¹⁸ The latest version of the procedure basically provides for a binding composition between a debtor and creditors, where a debtor's debts amount to less than R200 000,¹⁹ if accepted by the required majority in number and two-thirds in value of the concurrent creditors who vote on the composition.²⁰ It is clear that the procedure is aimed at negotiated settlements between parties. However, the *World Bank Report* expressed the sentiment that the benefits of such endeavours are mostly illusory.²¹

The debtor initiates the process by lodging a signed copy of the composition and a sworn statement with an administrator.²² Administrators are to supervise the

2000 Insolvency Bill sch 4. This proposal has also been included in the report of the Centre for Advanced Corporate and Insolvency Law (SACIL) at the University of Pretoria titled *Final report containing proposals on a unified Insolvency Act* (January 2000) and in the latest version of the Insolvency Bill; see cl 118 of the 2015 Insolvency Bill. In the last-mentioned document it is envisaged that the proposed measure should be included in the new unified Insolvency Act and not the Magistrates' Courts Act. The commission's initial proposal has also been amended in substance; see Roestoff and Jacobs 1997 *De Jure* 189 and Roestoff 2000 *De Jure* 131 *et seq* for discussions of the proposal in the 2000 Insolvency Bill. See further Steyn 2012 *PELJ* 220–222; Roestoff and Coetzee 2012 *SA Merc LJ* 70–71; Coetzee and Roestoff 2013 *Int Insolv Rev* 199–200 and Boraine and Roestoff 2014 *THRHR* 527–528 as regards a later draft of the procedure that was yet again amended to the effect contained in the 2015 Insolvency Bill.

¹⁶ Companies and close corporations are specifically excluded; cl 118(1).

¹⁷ Cl 118(1). The test to determine whether a debtor is 'unable to pay debts', as defined in s 2, includes the internationally-favoured liquidity test; ch 2 par 2.7.

¹⁸ See 2014 *Explanatory memorandum* 201 and 208.

¹⁹ Cl 118(1). There was no monetary threshold in the 2000 Insolvency Bill. It is not clear why the threshold was included especially since the credit industry is now accustomed to unlimited amounts of debt being restructured by means of the debt review procedure; see ch 4 par 4.3. Further, as the courts are not involved, jurisdictional issues could not be the reason therefor.

²⁰ Cl 118(17). Roestoff and Jacobs 1997 *De Jure* 195 and 207 submit that a mere majority in value and number is sufficient.

²¹ *WB Report* 46 *et seq*. See also ch 2 para 2.6.2.1 and 2.7. Nevertheless, it is in agreement with other (former) reports that if such measures are employed, certain elements may enhance its effectiveness. The fact that passive creditors are bound by the procedure, as is proposed in cl 118(17), is in line with international consensus; ch 2 par 2.7. The WB generally refers to settlement procedures as informal, even where they are regulated statutorily; *WB Report* 45 *et seq*. Other sources distinguish between formal and informal procedures on the basis of statutory regulation; see Fletcher *The law of insolvency* 45 and Josling 'Alternatives to bankruptcy' 10.47 and 10.48.

²² Cl 118(1). Such an offer may only be made once every six months. Once a composition is lodged, the debtor must not incur further debt without informing the prospective creditor of the pending composition and providing the insolvency practitioner with particulars concerning such debt; cl 118(3). It therefore seems that insolvency practitioners will act as intermediaries. A debtor must further not alienate, encumber or voluntarily dispose of assets that are made available to creditors in terms of the composition or act in any manner which can impede compliance therewith; cl 118(4).

procedure²³ and must determine a date for the questioning of the debtor and the consideration of the composition by creditors.²⁴ This will take place at a hearing.²⁵ The procedure provides that no creditor may without the court's permission institute any action against the debtor or apply for the liquidation of his estate between the determination of a date for a hearing and the conclusion thereof.²⁶ A moratorium on debt enforcement is in line with international principles, although it should become effective once a debtor applies for the procedure.²⁷ The administrator will preside at the hearing where claims will be proven²⁸ and, if needed, the debtor will be interrogated by the administrator, creditors and any other interested parties (with the permission of the administrator) as regards his assets, liabilities, present and future income (where applicable and including that of his spouse living with him), standard of living and the possibility of living more economically, and any other matter that the administrator may deem relevant.²⁹ Once the composition has been accepted,³⁰ the administrator must certify it as such and send the certificate to the master and creditors.³¹ After the certificate has been sent the composition is binding on all

²³ See cl 118 in general. An administrator must not be disqualified from being a liquidator in terms of s 69 (s 69, amongst others, requires that the administrator must be part of a professional body that is recognised by the minister); must have agreed to act as such; and must have furnished security to the satisfaction of the master; see cl 118(1). Obviously administrators would not be willing to set security where there is insufficient value in the estate to cover such costs. Administrators are entitled to remuneration payable in terms of the composition; cl 118(18)(c).

²⁴ Cl 118(6). The administrator may also, at any time on application by the debtor or an interested person, direct the debtor to appear for further questioning as the court may consider necessary on notice to creditors; cl 118(19)(a). The reference to 'court' is an obvious mistake.

²⁵ Cl 118(10). The hearing must proceed at a location that is accessible and convenient to creditors. The administrator must also inform creditors of the time, date and location of the hearing a least 14 days prior thereto; cl 118(7). The fact that the location must be accessible to creditors is not practical as various creditors with different domiciles may be involved. Furthermore, such provision may exclude many destitute debtors from applying for the procedure in instances where they need to travel and do not have the financial means to do so. It would be more appropriate to follow the debtor's domicile.

²⁶ Cl 118(23). Where the estate of the debtor was liquidated before he complied with the composition, creditors' claims are restored to the extent that they have not been satisfied; cl 118(21).

²⁷ Ch 2 par 2.7.

²⁸ See further cl 118(11)–(13). A creditor may by written power of attorney authorise any person to appear at the hearing on his behalf; cl 118(14).

²⁹ Cl 118(10)(e). The administrator may defer the hearing and the proposed composition may, with the debtor's permission, be amended or revoked; cl 118(15).

³⁰ A composition may not be accepted where a creditor shows, to the satisfaction of the administrator, that one creditor will benefit over another while he would not have been entitled thereto on liquidation of the debtor's estate; cl 118(16).

³¹ The administrator may revoke the composition in certain instances and may authorise the debtor, who on reasonable grounds is not able to comply therewith, to lodge an amended composition in accordance with cl 118(1); cl 118(19)(b). The provision for plan modification is in line with international principles and guidelines; ch 2 par 2.7. A composition may be revoked for the

Footnote continues on next page

creditors who received notice of or who have appeared at the hearing.³² However, the claims or rights of secured or preferent creditors are only subject to the composition if they consented thereto in writing.³³

If the required majority of creditors do not accept the composition and the debtor cannot pay substantially more than what is offered in the composition, the proposal is that³⁴

- (a) the administrator must declare that the proceedings in terms of this clause have ceased and that the debtor is once again in the position he or she was prior to the commencement thereof and lodge a copy of the declaration with the Master and known creditors by standard notice,³⁵ and

following reasons: Where the debtor fails to comply with obligations in terms of the composition; where the debtor renders false information in his statement or during his questioning; and where the debtor benefits a creditor who is not in terms of the composition entitled thereto; cl 118(19)(c). Any creditor entitled to a benefit in terms of the composition may, on 14 day's notice to the debtor, apply to the administrator to revoke the composition where the debtor does not comply therewith. Such creditor must lodge an affidavit in support of his application and the administrator must order the revocation if the debtor did not substantially comply with his obligations; cl 118(20). Once a composition is revoked, creditors' claims are restored to the extent that they have not been satisfied; cl 118(21).

³² Cl 118(17). After the composition has been accepted, the administrator must with six month intervals send an account of receipts, expenses and payments to creditors and the master; cl 118(17)(a). If the master is of the opinion that the account is incorrect, contains an improper charge or that the administrator has not acted in good faith or was negligent or unreasonable in incurring any costs in the account and that it should be amended, he may direct the administrator to do so and may further provide such directions in relation thereto as he may deem fit; cl 118(17)(b). The provisions of cls 89–92, 96(5), 96(7), 96(10) and (11) and 179 apply with the necessary amendments to an administrator; cl 118(17)(c). The clauses deal with bank accounts, investments, moneys belonging to the insolvent estate and estate accounts, distributions and contribution, except for cl 179 that deals with the review of proceedings. Cl 118(18)(a) provides that where provision is made for payment in instalments or otherwise, the composition has the effect of an order in terms of s 65 of the Magistrates' Courts Act in relation to such payments. Furthermore, any person who receives payments on behalf of creditors or a creditor who is entitled to benefit have the rights of a judgment creditor in terms of s 65; cl 118(18)(b).

³³ Cl 118(7). This feature accords with international principles and guidelines; ch 2 par 2.7.

³⁴ Cl 118(22). The commission's proposal in the 2000 Insolvency Bill afforded the debtor the option of converting to liquidation and rehabilitation in terms of the proposed Insolvency Act in instances where the composition was not accepted by the required majority. For criticism of this proposal see Roestoff and Jacobs 1997 *De Jure* 207 and Roestoff 2000 *De Jure* 131. The commentators, amongst others, submitted that the composition should lapse if not accepted by the required majority and that a debtor whose estate does not justify a *concurso creditorum* should fall back on existing debtors' remedies. This submission was made as the writers foresaw possible abuse of the procedure as it could be used as a tool to obtain a liquidation order by circumventing the advantage for creditors requirement in the voluntary liquidation procedure. The commentators' concerns have been addressed in the 2015 Insolvency Bill.

³⁵ In line with commentators' proposals; *ibid*.

- (b) the Master³⁶ may upon application by the debtor grant a discharge of debts of the debtor other than secured or preferred debts if—³⁷
- (i) the debtor satisfies the Master that the administrator and all known creditors were given standard notice of the application for the discharge with a copy of the debtor's application at least 28 days before the application to the Master; and
 - (ii) the Master is satisfied after consideration of the comments, if any, by creditors and the administrator and the application by the debtor –
 - (aa) that the proposed composition was the best offer which the debtor could make to creditors;
 - (bb) that the inability of the debtor to pay debts in full was not caused by criminal or inappropriate behaviour by the debtor;
 - (cc) that the debtor does not qualify to apply for an administration order in terms of section 74 of the Magistrates' Courts Act 32 of 1944.³⁸

In contrast to an administrator supervising the pre-liquidation procedure, the 2000 Insolvency Bill envisaged that the procedure would play out in the magistrates' courts. A commentator on the 2000 Insolvency Bill remarked that the officials of the magistrate's court are not suitably competent or experienced to deal with such a procedure and that they do not have the time or capacity needed for the successful administration thereof. The revised version of the procedure consequently makes provision for supervision by an administrator.³⁹ Even though the comment relating to the competence and experience of magistrates' courts was not without merit when the statement was made, it is submitted that officials of the magistrates' courts have been through a steep learning curve as they oversee the debt review procedure and rearrange unlimited amounts of debt originating from credit agreements governed by the NCA.⁴⁰ Therefore, the magistrates' courts are definitely in a better position to deal with these matters than in 2000. However, the comments in relation to time and capacity are still warranted. Furthermore, international principles and guidelines favour less court involvement.⁴¹ As was suggested in chapter 4,⁴² the national credit

³⁶ The master was decided upon as a court application would be too costly. A decision by the master is subject to review; 2014 *Explanatory memorandum* 209.

³⁷ The fact that the procedure provides for the possibility of formal procedures where negotiations fail is in line with international principles and guidelines; ch 2 par 2.7.

³⁸ It is odd that the debt review procedure in terms of the NCA is not mentioned; see ch 4 par 4.3 as regards the debt review procedure.

³⁹ 2014 *Explanatory memorandum* 202.

⁴⁰ See ch 4 par 4.3.

⁴¹ Ch 2 par 2.7.

⁴² Par 4.2.8.

regulator⁴³ could be considered as a supervising body as regards alternative debt relief measures.

Of especial importance to this thesis is the fact that the proposed procedure may provide the presently excluded no income and no assets debtors (the so-called NINA debtors) with a route to a discharge. In fact, the 2014 *Explanatory memorandum* submits that, in line with international developments in insolvency law, the procedure is intended to afford those who do not qualify for liquidation proceedings ‘an opportunity for a fresh start which entails a discharge of debts’.⁴⁴ However, although sub-clause 22 was probably inserted with the NINA category of debtors in mind, it is most certainly not suited to their needs. The major problem with the procedure in relation to NINA estates is that it does not make sense to force such debtors through its negotiation phase as they do not have any negotiating power due to the fact that they do not own anything of value which they can offer. Also, as negotiations are doomed from the outset, the costs involved, for instance that of the administrator and insolvency practitioner as well as travelling expenses (as credit providers’ domiciles need to be followed), in employing the first part of the procedure will all be for naught. Furthermore, NINA debtors are in any event not in a position to finance the procedure and no provision is made for free assistance to these debtors.⁴⁵ It is acknowledged that the initiative is commendable and that its implementation would be ground-breaking. However, it will unfortunately not provide an effective debt relief measure for NINA estates.

5.3 The *in duplum* rules

An *in duplum* rule can be regarded as a type of debt relief instrument as it assists a defaulting debtor, who will more often than not also be in financial distress, to establish a moratorium on the further accumulation of certain costs under certain circumstances. Two *in duplum* rules are found in South African law. The one stems from the common law and the other from section 103(5) of the NCA. As will be seen

⁴³ Hereafter the ‘NCR’. See the discussion of the NCR in ch 4 par 4.3.2.

⁴⁴ 2014 *Explanatory memorandum* 208.

⁴⁵ In contrast with international principles and guidelines; ch 2 par 2.7.

from the discussion below, the statutory rule affords broader protection and relief than the common law rule.⁴⁶

The common law *in duplum* rule⁴⁷ originates from Roman law and has the effect that once a consumer is in *default* in terms of the repayment of a loan, the accumulation of arrear and unpaid interest whilst the debtor is in default may not exceed the outstanding capital amount at the date of the default. The common law *in duplum* rule is therefore only concerned with interest and takes effect once the consumer is in default. When the debtor makes a payment it will firstly be appropriated to interest and thereafter to capital. However, once the consumer makes a payment, thereby reducing the amount of arrear interest below the amount of the outstanding capital, the interest can again run up to the outstanding capital amount. It thus has a gyrating effect and the moratorium will only become effective again when the arrear and outstanding interest again reach the outstanding capital amount. The rule is suspended on the service of a summons, with the result that interest may start to run afresh.

The statutory *in duplum* rule⁴⁸ only applies to credit agreements as defined by the NCA and is subject to additional jurisdictional provisions.⁴⁹ It provides as follows:⁵⁰

Despite any provision of the common law or a credit agreement to the contrary, the amounts contemplated in section 101(1)(b) to (g)⁵¹ that accrue during the

⁴⁶ See *Nedbank Ltd v National Credit Regulator* 2011 (3) SA 581 (SCA) 603 where the Supreme Court of Appeal quoted with approval from Kelly-Louw 2007 SA Merc LJ 344. See Otto 2012 THRHR 127 for a discussion of the case. See also Eiselen 2012 THRHR 398 *et seq.* For discussions of the statutory *in duplum* rule see Van Zyl 'Interest, fees and charges' 10.6.4; Kelly-Louw and Stoop *Consumer credit regulation* 254–261; Campbell 2010 SA Merc LJ 4 and Kelly-Louw 2011 SA Merc LJ 352. See also GN 54 in GG 38419 of 30 January 2015 regarding proposed guidelines issued by the NCR for the interpretation of the statutory *in duplum* rule.

⁴⁷ See, amongst others, *LTA Construction Bpk v Administrateur Transvaal* 1992 (1) SA 473 (A) 482; *Commissioner for SA Revenue Service v Woulidge* 2000 (1) SA 600 (C) 611; *National Credit Regulator v Nedbank* 2009 (6) SA 295 (GNP) 319; *Nedbank Ltd v National Credit Regulator* 599–601 and authorities cited there; Van Zyl 'Interest, fees and charges' 10.6.4; and Kelly-Louw and Stoop *Consumer credit regulation* 251–254 for discussions of the common law *in duplum* rule. See further Vessio 2006 *De Jure* 25. See also Sonnekus 2012 TSAR 247 as regards the historical development of the rule.

⁴⁸ This rule became operative on 1 June 2007; proc 22 in GG 28824 of 11 May 2006. The rule does not apply to agreements entered into before the effective date; item 4(2) sch 3 of the NCA.

⁴⁹ The statutory rule does not apply to agreements where the consumer is a juristic person; s 6(d). See ch 4 par 4.3.1 for a general discussion of the application of the NCA.

⁵⁰ S 103(5).

⁵¹ S 101 is headed 'Cost of credit' and provides that a credit agreement must not require payment of any money or other consideration except as provided for in the section. S 101(1)(a) refers to

Footnote continues on next page

time that a consumer is in default under the credit agreement may not, in aggregate, exceed the unpaid balance of the principal debt⁵² under that credit agreement as at the time that the default occurs.

The Supreme Court of Appeal held that the statutory *in duplum* rule is not a codification of the common law rule.⁵³ The court determined that the rule is⁵⁴

a statutory provision with limited operation. It seeks not only to amend the common-law *in duplum* rule but also to extend it. It deals with the same subject-matter as the common-law rule but this does not mean that it incorporates all or any of the aspects of the common-law rule. It is a self-standing provision and must be construed as such.

Consequently, debtors who do not enjoy the greater protection of the statutory *in duplum* rule are still protected by the common law rule.

The statutory rule prescribes that the accrual of all costs of credit combined is stayed once it reaches the outstanding principal debt. In *National Credit Regulator v Nedbank Ltd*, Du Plessis J interpreted the statutory rule as prescribing that the amounts specified in section 101(1)(b)–(g), accruing whilst the consumer is in default, may not in aggregate exceed the unpaid principal balance when the default occurred; that once the total charges as contemplated in section 101(1)(b)–(g) equal the unpaid balance, no further charges may be imposed; and that once the total charges as provided for in section 101(1)(b)–(g) reach the amount of the unpaid balance, payments made by the consumer whilst still in default do not allow the credit provider to charge further interest whilst the consumer is still in default.⁵⁵ On appeal, the Supreme Court of Appeal concurred with the court *a quo* and confirmed that, in terms of the statutory rule, the accrual of interest and other costs combined

the principal debt deferred in terms of the agreement, whilst s 101(1)(b)–(g) provides for costs other than the principal debt. These are an initiation fee, a service fee, interest, the cost of any credit insurance as provided for in the NCA, default administration charges and collection costs.

⁵² S 101(1)(a) provides that 'principal debt' refers to the amount deferred in terms of the credit agreement plus the value of items as contemplated in s 102. S 102 provides for fees or charges that may be capitalised under specified circumstances where the agreement qualifies as an instalment agreement, a mortgage agreement, a secured loan or a lease.

⁵³ For a useful and practical explanation and comparison of the two rules see Kelly-Louw 2011 SA *Merc LJ* 352.

⁵⁴ *Nedbank Ltd v National Credit Regulator* 601.

⁵⁵ *National Credit Regulator v Nedbank Ltd* 321.

may only resume once the consumer is no longer in default.⁵⁶ In other words, even where the consumer makes payments, thereby reducing the outstanding debt, it does not have the effect (as is the case in terms of the common law rule) of allowing the credit provider to charge further costs until the consumer is no longer in (any) default.⁵⁷ Further, where the operation of the common law rule is suspended by the service of a summons, the only condition for the statutory rule's continuation is that the consumer must be in default. Legal processes therefore do not have any effect thereon.⁵⁸ When considering the statutory *in duplum* rule's attributes, it is apparent that it could in certain circumstances save an already destitute debtor from further financial turmoil.

Kelly-Louw submits that although it is not the duty of a court to raise the defence of the common law *in duplum* rule, the court should always consider the application of the statutory rule.⁵⁹ Therefore, also in (any) insolvency proceedings, courts should take cognisance of the workings of section 103(5).

⁵⁶ Kelly-Louw and Stoop submit that a consumer will no longer be in default once he has repaid all arrear interest, costs of credit and the capital amount that he would have paid if he had not defaulted on the agreement; Kelly-Louw and Stoop *Consumer credit regulation* 260 n257.

⁵⁷ *Nedbank Ltd v National Credit Regulator* 606–607. Otto 2012 *THRHR* 130–131 submits that the consequence of this decision is that a consumer whose total sum of arrear interest, services fees, insurance premiums, *etcetera* has reached the balance of the principal debt during periods of default need not pay any further amounts in connection with these fees and charges. If he starts paying his debt again, the payments will be allocated to the outstanding principal debt only.

Eiselen 2012 *THRHR* 400 states that it is inconceivable that the decision could have meant that payments could be allocated in any other way than by first reducing the outstanding cost of credit and then capital as prescribed by section 126(3). To allocate payments only to capital will mean that the interest and other charges in arrears can in effect never be claimed. Such an interpretation is not only an absurdity, but makes nonsense of section 103(5) itself and creates an unequal position in regard to consumers who are in arrears but who have not 'achieved' *in duplum* yet.

Friedman and Otto 2013 *THRHR* 143 state that as regards the impact of s 126(3) on s 103(5) the statement of the Supreme Court of Appeal in *Nedbank Ltd v National Credit Regulator* 606, that payments made during the time of default, which do not end the default, simply reduce the outstanding principal debt

cannot be correct in respect of the amounts which accrued from the time of the initial default until the double was reached, as these amounts remain outstanding and any payments made should be allocated in accordance with section 126(3). Only once these amounts have been settled would this remark be correct.

⁵⁸ *Nedbank Ltd v National Credit Regulator* 601–602 and 607. See Kelly-Louw and Stoop *Consumer credit regulation* 260.

⁵⁹ See the discussion in Kelly-Louw 2011 *SA Merc LJ* 369–370.

5.4 Court-ordered debt review

It has been established that the debt review procedure coupled with the possibility of debt restructuring in terms of the NCA in some instances provide South African consumers with an alternative debt relief measure as opposed to sequestration in terms of the Insolvency Act.⁶⁰ In this regard the conventional route of employing the procedure has been considered.⁶¹ However, section 85 of the NCA provides the consumer, in the context of the NCA and through court involvement, with two substitute routes towards a possible re-arrangement of his obligations in terms of section 87⁶² of the NCA. Section 85 reads as follows.⁶³

Despite any provision of law or agreement to the contrary, in any court proceedings in which a credit agreement is being considered, if it is alleged that the consumer under a credit agreement is over-indebted, the court may—

- (a) refer the matter directly to a debt counsellor with a request that the debt counsellor evaluate the consumer's circumstances and make a recommendation to the court in terms of section 86(7); or
- (b) declare that the consumer is over-indebted, as determined in accordance with this Part, and make any order contemplated in section 87 to relieve the consumer's over-indebtedness.

Even though section 88 has been discussed in the context of the debt review procedure in chapter 4,⁶⁴ it is also relevant to the present discussion and the discussion relating to reckless credit in the following paragraph.⁶⁵ The relevant parts of the section provide that when it is alleged in court that a consumer is over-indebted, he must not incur further charges under a credit facility or enter into further credit agreements,⁶⁶ other than consolidation agreements, with any credit provider until one of three events has occurred.⁶⁷ These are set out in section 88(1), namely, that

⁶⁰ 24 of 1936. See ch 4 par 4.3 for a detailed discussion and investigation of the debt review procedure in relation to the relief that it offers.

⁶¹ S 86.

⁶² See ch 4 par 4.3.2 for a discussion of s 87.

⁶³ For discussions of s 85 see Kreuser 2012 *De Jure* 1 and Van Heerden 2013 *De Jure* 968. See also Van Heerden 'Over-indebtedness and reckless credit' 11.3.3.5; Otto and Otto *NCA explained* 30.9; and Kelly-Louw and Stoop *Consumer credit regulation* 382–392.

⁶⁴ At par 4.3.2.

⁶⁵ Par 5.5.

⁶⁶ Where a credit provider enters into a credit agreement, other than a consolidation agreement, and where a consumer has applied for a debt re-arrangement and whilst such re-arrangement subsists, all or part of the agreement may be declared as reckless credit irrespective of whether s 80 is applicable; s 88(4).

⁶⁷ Where a consumer applies for or enters into a credit agreement in contravention of s 88, the provisions of ch 4 pt D will never apply to such an agreement; s 88(5).

- (a) [t]he debt counsellor rejects the application and the prescribed time period for direct filing in terms of section 86(9) has expired without the consumer having so applied;
- (b) the court has determined that the consumer is not over-indebted, or has rejected a debt counsellor's proposal or the consumer's application; or
- (c) a court having made an order or the consumer and credit providers having made an agreement re-arranging the consumer's obligations, all the consumer's obligations under the credit agreements as re-arranged are fulfilled, unless the consumer fulfilled the obligations by way of a consolidation agreement.⁶⁸

In turn, section 88(3)⁶⁹ is concerned with a credit provider's prohibited conduct once he has received notice of court proceedings as contemplated in sections 83⁷⁰ or 85 or a notice in terms of section 86(4)(b)(i).⁷¹ It provides that such a credit provider may not exercise or enforce by litigation or other judicial process any right or security under such an agreement until –⁷²

- (a) the consumer is in default under the credit agreement; and
- (b) one of the following has occurred:
 - (i) An event contemplated in subsection (1)(a) through (c); or
 - (ii) the consumer defaults on any obligation in terms of a re-arrangement agreed between the consumer and credit providers, or ordered by a court or the Tribunal.⁷³

It is evident from the wording in section 85 that two basic prerequisites should be met before a court may exercise its discretion in terms of section 85. The first is that a credit agreement⁷⁴ should be under consideration in any court proceedings⁷⁵ (action or application proceedings in the high or magistrate's court)⁷⁶ and the second

⁶⁸ Where a consumer's obligations are fulfilled by way of such a consolidation agreement, the effect of s 88(1) continues until the consumer has fulfilled his obligations under such an agreement unless the consumer again fulfils the obligations through a consolidation agreement; s 88(2).

⁶⁹ The subsection is subject to s 86(9) and 86(10).

⁷⁰ See par 5.5.

⁷¹ See ch 4 par 4.3.2.

⁷² This section is in line with international guidelines as regards a moratorium on creditors' actions against the debtor whilst a solution is being sought. It also helps to ensure fair treatment amongst creditors; ch 2 par 2.7.

⁷³ The National Credit Tribunal was established by s 26 of the NCA. It is a juristic person with jurisdiction throughout the country. Even though it is not a court, it functions in a similar fashion in that it adjudicates matters in terms of the NCA; ss 26 and 27.

⁷⁴ Such an agreement should obviously be one to which the NCA applies. See ch 4 par 4.3.1 for a discussion of the NCA's field of application.

⁷⁵ See *Ex parte Ford* 2009 (3) SA 376 (WCC) 381 where it was held that the wording 'in any court proceedings' affords the clearest indication as regards the intended wide ambit of the section's operation. See ch 3 par 3.3.2.3 for a discussion of the case.

⁷⁶ See *Standard Bank of South Africa Ltd v Panayiotts* 2009 (3) SA 363 (W) 367–368 where it was held that where a high court referred the matter to a debt counsellor, the high court should

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is that the consumer's over-indebtedness should be alleged.⁷⁷ Even though consumers mostly make use of section 85 once enforcement proceedings have already been instituted and may do so in a pleading, affidavit or even *viva voce*,⁷⁸ there seems to be no objection against the consumer invoking the section by means of a substantive application.⁷⁹ However, invoking section 85 does not amount to defending a claim and usually takes the form of a request to the court to exercise its powers in terms thereof.⁸⁰ As an allegation of over-indebtedness is the second prerequisite, the court in *FirstRand Bank Ltd v Maleke*⁸¹ acknowledged that it cannot *suo motu* exercise its powers where no such allegation was made. However, a court may act *suo motu* where the two statutory prerequisites are present.⁸²

Even though section 85 is worded in very wide terms and only requires the above two factors to be present as conditions for invoking it, the question arises whether it may be raised in all instances where the two prerequisites are present. In this regard, Binns-Ward J in *Standard Bank of South Africa Ltd v Kallides*⁸³ came to the following conclusion:

Notwithstanding the breadth of the opening words to s 85 of the NCA, reference to the broader context of the statute impels the conclusion that the section was not intended to provide a basis for a repetition of the process already provided for in terms of s 86, or to draw back within the ambit of debt review debts already excluded therefrom by the operation of other provisions of the Act, such as s 86(2), s 86(10) or s 88(3). To construe s 85 otherwise would be conducive to the most unwholesome circularity, at odds with the basic principle – *interest rei publicae ut sit finis litium*.⁸⁴

receive the debt counsellor's recommendation and deal with the matter in terms of s 86(7)(c). This is so as s 85(a) in contrast with s 86(7)(c) refers to 'court' which includes both the magistrate's court and the high court and that an interpretation that only the magistrate's court can entertain such matters would lead to absurdity as a magistrate's court would then adjudicate a matter pending in the high court. The court further mentioned that the element of policing would also be a problem since the high court would not ordinarily know whether its request has been heeded and followed through in the magistrate's court.

⁷⁷ *Idem* 367.

⁷⁸ *Standard Bank Ltd v Kallides* unreported case nr 1061/2012 (WCC) par 6.

⁷⁹ Van Heerden 2013 *De Jure* 978.

⁸⁰ *Standard Bank of South Africa Ltd v Hales* 2009 (3) SA 315 (D) 320 and *Collett v FirstRand Bank Ltd* 2011 (4) SA 508 (SCA) 518. For a discussion of *Standard Bank of South Africa v Hales* see Van Heerden and Lötze 2010 *THRHR* 502.

⁸¹ 2010 (1) SA 143 (GSJ) 157. See also *Standard Bank of South Africa v Panayiotts* 368.

⁸² *Standard Bank Ltd v Kallides* par 6.

⁸³ *Idem* 8.

⁸⁴ Loosely translated as 'it is in the interest of the state that litigation be finalised'; Hiemstra and Gonin *Drietalige regswoordeboek* 211.

The Supreme Court of Appeal in *Seyffert v FirstRand Bank Ltd*⁸⁵ referred to the above conclusion and held that it is too absolute and loses sight of the court's discretion as provided for by the word 'may' and the words commencing the section, namely, '[d]espite any provision of law or agreement to the contrary'. However, the court, with reference to *Hales*,⁸⁶ further stated that before a court can exercise its discretion in terms of section 85, the material facts relied upon must be placed before it.⁸⁷ It further held that a court should be slow to exercise its discretion where the matter has already been dealt with by a debt counsellor or where a debt review has been duly terminated and where no material change in the debtor's circumstances can be shown. Nevertheless, in the case under consideration the proposals were not viable and the court therefore did not exercise its discretion in favour of the consumers.⁸⁸ The court recognised that section 86(10)⁸⁹ has its own balancing provision in the form of section 86(11)⁹⁰ and that the appellants did not apply for a resumption in terms of the latter section.⁹¹ However, the fact that another procedure may be available to the consumer and may even be better suited to or specifically created for his circumstances was not regarded by the court as an absolute hindrance to invoking the section 85 procedure.

In considering the circumstances for which section 85 was intended, the comments and insights of Van Heerden are significant. She refers to three scenarios where a consumer might be interested in invoking section 85 post-enforcement – as she is of the opinion that it could not have been the intention of the legislature that section 86(2) should bar a consumer from utilising section 85 in an attempt to access the debt review process for the first time.⁹² As the more economical port in terms of

⁸⁵ 2012 (6) SA 581 (SCA) 587. See Steyn 2012 *De Jure* 639 for a discussion of the judgments of both the court *a quo* and the Supreme Court of Appeal in the context of the NCA's inability to adequately address issues pertaining to execution against debtors' mortgaged homes.

⁸⁶ 321–322.

⁸⁷ *Seyffert v FirstRand Bank Ltd* 587.

⁸⁸ *Ibid.*

⁸⁹ See ch 4 par 4.3.2.

⁹⁰ *Ibid.*

⁹¹ *Seyffert v FirstRand Bank Ltd* 585–586.

⁹² Van Heerden 2013 *De Jure* 977. See in this regard *Nedbank Ltd v The National Credit Regulator* and the criticism of the decision in ch 4 par 4.3.3. At the time that Van Heerden made the submissions, the delivery of a s 129(1)(a) notice excluded the specific agreement in terms of which it was sent from the debt review process. This situation has changed in light of the amendment to s 86(2) which now refers to s 130 and not to s 129; s 26(a) National Credit Amendment Act 19 of 2014 (hereafter 'the Amendment Act'); see ch 4 par 4.3.2.

section 86 is still available to consumers before a credit provider has taken steps to enforce a credit agreement,⁹³ it is highly unlikely that such consumers will bring court applications in order to bring their situations within the ambit of section 85. The first situation described by Van Heerden is where the consumer did not previously apply for the debt review procedure; the second is where the consumer did apply for the debt review procedure, but where the credit provider proceeded with enforcement without terminating the procedure as provided for in section 86(10); and the third is where a debt review procedure has been terminated in accordance with section 86(10) but where the credit provider did not act in good faith.⁹⁴ Van Heerden submits that the NCA provides specific procedures to be utilised by an aggrieved consumer in the last two scenarios. In the third scenario, she argues that section 86(11) provides the suitable remedy which is distinct from section 85 in its purposes and that section 85 is therefore not applicable. Where the credit provider did not terminate a pending debt review prior to enforcement, as is prescribed by section 86(10), and then proceeds to enforce the agreement, section 130(4)(c)⁹⁵ provides the proper remedy and section 85 is also not suited to such instances.⁹⁶ Van Heerden consequently reaches the conclusion that the scope of application of section 85 is confined to instances where there was no application for debt review prior to the commencement of enforcement proceedings. Accordingly, section 85 is only available to consumers who did not or who were unable to make use of the section 86 procedure.⁹⁷ It is therefore suggested that the measure acts as an ‘abuse-filter’ in instances where there was no prior application for debt review.⁹⁸ Van Heerden’s conclusion is in part contrary to the sentiments expressed by Binns-Ward J in *Standard Bank of South Africa Ltd v Kallides*⁹⁹ as quoted above and mostly different from the opinion of the Supreme Court of Appeal in *Seyffert v FirstRand*

⁹³ See ch 4 par 4.3.3.

⁹⁴ Van Heerden 2013 *De Jure* 973.

⁹⁵ S 130(4)(c) provides that in any proceedings as contemplated in s 130, where a court determines that a credit agreement is subject to a pending debt review in terms of ch 4 part D, the court may

- (i) adjourn the matter, pending a final determination of the debt review proceedings;
- (ii) order the debt counsellor to report directly to the court, and thereafter make an order contemplated in s 85(b); or
- (iii) if the credit agreement is the only credit agreement to which the consumer is a party, order the debt counsellor to discontinue the debt review proceedings, and make an order contemplated in s 85(b).

⁹⁶ Van Heerden 2013 *De Jure* 973–975.

⁹⁷ *Idem* 975–976.

⁹⁸ Van Heerden 2013 *De Jure* 977.

⁹⁹ Par 8.

*Bank Ltd.*¹⁰⁰ However, even though the Supreme Court of Appeal awarded the utmost breadth of application to section 85, it is submitted that Van Heerden's suggestions and to some extent also that of Binns-Ward J are valuable where courts have to exercise their discretion in terms of section 85. As was pointed out above, section 86(10) has its own balancing provision in the form of section 86(11), which was also recognised by the Supreme Court of Appeal in *Seyffert*. Both Van Heerden and Binns-Ward J are of the opinion that section 85 is not competent in instances where a section 86(10) termination has been effected. It is thus submitted that when a court is considering whether to exercise its section 85 discretion under such circumstances it should take into account the fact that the consumer did not follow the section 86(11) procedure, and in instances where the consumer has invoked section 85 (as opposed to where the court considers its section 85 discretion *suo motu*) it should request reasons for such failure. Where the credit provider did not duly terminate a debt review prior to commencing debt enforcement, the court should consider the provisions of section 130(4)(c). It is submitted that in such instances the powers of the court, as provided for in section 130(4)(c), can be combined with that of section 85 which will provide the court with more options.

As far as section 88(3) is concerned, it has been pointed out above that it deals with the prohibition to enforce a credit agreement once a credit provider has received notice of certain proceedings, and before certain prescribed factors are present. The section therefore places a moratorium on enforcement until such events have occurred. Binns-Ward J held¹⁰¹ that after the events as provided for in section 88 have lifted the moratorium, a credit provider may proceed to enforce the agreement and that the section 85 remedy would not be competent thereafter. Under such circumstances and according to Binns-Ward J¹⁰² the consumer already had his 'chance' in that a debt counsellor has rejected the application and the consumer did not approach the court during the grace period; a court has determined that the consumer is not over-indebted or has rejected a debt counsellor's proposal or a consumer's application; or a re-arrangement order or agreement has been made and all of the consumer's obligations in terms thereof are fulfilled. It is submitted that

¹⁰⁰ 587.

¹⁰¹ *Standard Bank Ltd v Kallides* par 6.

¹⁰² *Idem* 8.

where section 88 is applicable to the circumstances under a court's consideration, the court should take cognisance of its provisions and their purposes in considering whether to exercise its discretion in terms of section 85. A relevant factor resonating from section 88 could for instance be that the court has already rejected a proposal or an application for debt review. In such circumstances and absent pressing reasons to provide the consumer with yet another bite at the cherry, the court should not exercise its discretion in favour of the consumer. However, where section 88 is applicable to the circumstances under consideration but the consumer is not at fault because the debt counsellor was for instance reckless in the preparation of the debt review application, this factor should weigh in the consumer's favour.

As far as Binns-Ward J's reference to section 86(2) is concerned, it is agreed with Van Heerden that it could not have been the intention of the legislature to, in all instances, exclude agreements where debt enforcement has commenced from a possible re-arrangement. It is submitted that this could even have been the exact circumstances that the legislature had in mind when drafting section 85. It could be that the legislature intended that agreements where enforcement has commenced should be excluded as a matter of course (through the section 86(2) provision), but that such agreements may be included in the discretion of a court where the circumstances and reason necessitate their inclusion. Further, should one accept that Binns-Ward J is correct in excluding agreements where enforcement proceedings have commenced, it is difficult to contemplate a situation where a *bona fide* consumer would be able to make use of the section 85 remedy as section 86 is still available to (and probably preferred by) the consumer up to such point – as was noted by Van Heerden.¹⁰³

Van Heerden notes¹⁰⁴ that in addition to the considerations mentioned above, the court should also take cognisance of the manner in which the credit provider has proceeded with enforcement proceedings. A situation where the consumer has been in default for quite some time and has been contacted by the credit provider in relation thereof prior to the credit provider taking steps to enforce the agreement

¹⁰³ See Van Heerden 2013 *De Jure* 977.

¹⁰⁴ *Idem* 990–991.

should be contrasted with a situation where a credit provider has immediately and as a matter of course proceeded to enforce the agreement once the consumer was in default.¹⁰⁵

Further relating to the court's discretion,¹⁰⁶ it should be exercised judicially¹⁰⁷ and with due regard to the objectives of the NCA, as set out in section 3, and other relevant sections which are intended to provide a backdrop against which the discretion must be exercised.¹⁰⁸ The fact that the court must exercise its discretion judicially means that it should be exercised for substantial reasons and on the material before it and not capriciously, on the basis of conjecture or speculation or upon wrong principles.¹⁰⁹ Therefore, the party requesting the court to exercise its discretion should place as much as possible relevant material before the court to assist it in its task.¹¹⁰ As regards the court's discretion within the ambit of section 85, Kreuser argues that the NCA brought about a wave of consumer protection and that '[t]he legislature saw a need for debt alleviation and introduced debt counselling as a solution to the over-indebtedness problem'.¹¹¹ She also submits that section 85 was drafted for the protection of consumers and that the debt relief measures of the NCA must be used to achieve their objective. Kreuser concludes that

[e]ach case must be assessed on its merits and, as far as possible and reasonable, be decided in favour of the consumer.

Thus far, no judgment has been reported in which the second orders that a court may make, namely, to declare the consumer over-indebted and to make an order as contemplated in section 87, were considered. This may be attributed to the fact that most matters involve various credit agreements and that an investigation into

¹⁰⁵ *Ibid.*

¹⁰⁶ *Seyffert v FirstRand Bank Ltd* 587.

¹⁰⁷ See *Standard Bank of South Africa Ltd v Hales* 321; see also *Standard Bank of South Africa v Panayiotis* 372 and *Andrews v Nedbank Ltd* 2012 (3) SA 82 (ECG) 87.

¹⁰⁸ *Standard Bank of South Africa Ltd v Hales* 321; *FirstRand Bank Ltd v Olivier* 2009 (3) SA 353 (SE) 359; and *Andrews v Nedbank Ltd* 87. For a discussion of *FirstRand Bank Ltd v Olivier* see *Otto* 2009 SA Merc LJ 272.

¹⁰⁹ See *Standard Bank of South Africa Ltd v Hales* 321 where the court refers to *Myburgh Transport v Botha* 1991 (3) SA 310 (Nms) 314 and *First National Bank of SA Ltd v Myburg* 2002 (4) SA 176 (C) 184.

¹¹⁰ See *Standard Bank of South Africa Ltd v Hales* 321. Van Heerden 2013 *De Jure* 989–990 sets out the information needed to enable a court to exercise its discretion judicially and to make sure that the consumer is not raising his over-indebtedness in order to delay with no real intention or probable prospect of obtaining debt relief and eventually satisfying his obligations. See below.

¹¹¹ Kreuser 2012 *De Jure* 21.

consumers' financial affairs, negotiations with credit providers and the arithmetic involved in such endeavours should rather be left to debt counsellors whose core business involves such functions as opposed to the courts who have a judicial role to play.¹¹²

Conversely, many decisions have considered the first order, namely, that the court may refer the matter to a debt counsellor requesting the latter to evaluate the consumer's circumstances and thereafter make a recommendation to the court in terms of section 86(7). Even though the section does not require proof of over-indebtedness before such an order may be made, it was held in *Hales*¹¹³ that the *fact* of over-indebtedness as opposed to an allegation thereof should be taken into account when the court exercises its discretion.¹¹⁴ In *Olivier*¹¹⁵ counsel for the credit provider submitted that certain further factors are relevant to and could influence the exercise of the court's discretion. These are the fact that the consumer did not apply to a debt counsellor in terms of section 86(1) to have himself declared over-indebted; the consumer's failure to explain why he did not approach a debt counsellor prior to enforcement; and the fact that the consumer awaited enforcement proceedings rather than taking voluntary steps to be declared over-indebted which according to the credit provider amounted to an abuse of process. In the latter regard it was further submitted that the following factors also pointed to abuse:

- (a) The NCA provides a simple, inexpensive and effective procedure for debt restructuring in s 86.
- (b) These provisions were obviously designed to expedite and to simplify the procedure relating to debt restructuring.
- (c) These procedures are furthermore designed to avoid the necessity of the parties having to resort to the far more costly procedure of applying to the High Court for relief.
- (d) It is also undesirable that the High Court has to deal with frequent applications for debt restructuring, very much along the lines of a court sitting in terms of s 65 of the Magistrates' Courts Act, Act 32 of 1944.

¹¹² See Van Heerden 2013 *De Jure* 990–992 for the aspects relevant to the exercise of the court's discretion in this regard.

¹¹³ 322.

¹¹⁴ In *Standard Bank of South Africa v Panayiotis* 368 and 373 it was held that over-indebtedness should be established on a balance of probabilities.

¹¹⁵ 359.

The court accepted that such considerations could in appropriate circumstances influence the court in the exercise of its discretion.¹¹⁶ In *Hales*, in turn, the consumer purported to apply for debt review in terms of section 86 after the application for summary judgment had been delivered. The credit provider raised the factors referred to in *Olivier* and in addition set out further factors that it argued the court should take into account. These are that:¹¹⁷

- (1) there was no explanation for the delay in their application for debt review in terms of s 86;
- (2) there was no explanation for the dishonest defence raised in the affidavit opposing summary judgment;¹¹⁸
- (3) the defence raised is clearly designed to frustrate the plaintiff in obtaining judgment and foreclosing on the immovable property;
- (4) if one deducts from the monthly expenses of the defendants that (sic) amount required to service the mortgage bond, the defendants would be living within their means and would not be over-indebted; and
- (5) the defendants had not paid any instalments for a period of some 14 months.

Counsel for the credit provider further argued that since the defendants did not timeously take the steps set out in section 86(1) after receiving a notice in terms of section 129(1)(a), the invocation of section 85(a) amounted to an abuse of process. The court did not agree with this argument and provided various practical reasons why it is not necessarily the case.¹¹⁹ However, the consumers did not provide the court with sufficient information regarding the circumstances which brought them to rely on section 85(a), such as the reason for their default; what they did to remedy their financial problems; why they did not timeously apply to a debt counsellor to be declared over-indebted; details regarding their expenditure especially relating to their other indebtedness; and whether it would be feasible to reschedule their debt. The court pointed to the fact that the defendants abruptly stopped paying their instalments and that it did not seem that there was much potential for successfully rescheduling the indebtedness under the mortgage bond.¹²⁰ The court also referred to the fact that if judgment was granted in favour of the credit provider a substantial portion of the consumers' monthly burden would be relieved. Another factor that the

¹¹⁶ *Ibid.*

¹¹⁷ *Standard Bank of South Africa Ltd v Hales* 324.

¹¹⁸ This is a defence that the consumers did not receive a s 129(1)(a) notice, which was raised in opposing the application for summary judgment; 325.

¹¹⁹ *Ibid.*

¹²⁰ *Idem* 325.

court found to be relevant to the exercise of its discretion was that the credit provider had complied with the provisions of the NCA and went even further in not approaching the court as soon as it was entitled to do so.¹²¹ Judgment was consequently granted in favour of the credit provider.¹²²

Van Heerden refers to the aforementioned cases and notes that they illustrate that, in order to assist the court to exercise its discretion judicially and to ensure that the consumer does not merely raise over-indebtedness as a delaying tactic with no true intention or feasible prospect of obtaining relief and eventually satisfying all obligations, the consumer must at a minimum disclose the following information to the court:¹²³

- (a) facts that indicate that the consumer is *probably* over-indebted
- (b) an acceptable explanation of why the consumer did not access the voluntary debt review process prior to delivery of the section 129(1)(a)-notice (Here the credit provider's conduct may be relevant eg that the credit provider sent a section 129(1)(a)-notice immediately upon default and refused to entertain any submissions by the consumer)
- (c) detail of how the consumer became over-indebted
- (d) the consumer must provide details of any payments or debt repayment proposals or debt restructuring proposals he has made to the credit provider or any other interactions he had with the credit provider in an attempt to address his default and debt position
- (e) details of the consumer's total debt situation
- (f) details of the consumer's income
- (g) the stage of the proceedings at which section 85 is invoked (a consumer who is over-indebted and genuinely wishes to access debt relief via debt review will usually at least raise the issue at summary judgment stage – if it is raised at a much later stage such as at trial, the court should consider the possibility of abuse)
- (h) a reasonable explanation as to why he did not access the voluntary debt review procedure (for example because the credit provider acted promptly upon his the (sic) consumer's first default and sent him a section 129(1)(a)-notice before he could approach a debt counsellor)
- (i) facts that indicate that his financial position is such that in all probability the debt counsellor who conducts the debt review will be able to come up with an economically feasible debt rescheduling proposal.

¹²¹ *Idem* 326.

¹²² *Idem* 328.

¹²³ Van Heerden 2013 *De Jure* 989–990.

Van Heerden submits that all the above factors play a role, but that, in the absence of abuse, the possibility of an economically feasible restructuring is of utmost importance in the court's exercise of its discretion in terms of section 85(a).¹²⁴

Van Heerden suggests that if the court decides to exercise its powers in terms of section 85(a) it will in all probability postpone the proceedings (in which the section 85 proceedings were invoked), pending the debt counsellor's recommendation. Except where the court indicated the date by which the debt counsellor should make its recommendation to court, the debt counsellor should follow the same procedure as provided for in section 86.¹²⁵ If the proceedings in terms of section 85(a) read together with section 86(7) are for any reason properly brought to an end, the original proceedings may proceed. Van Heerden submits that this situation differs from the powers of the court where the second order is competent. In such instances the court will be able to make any order as contemplated in section 87 to relieve the consumer's over-indebtedness. Once such an order is made, section 88(3) becomes relevant and a credit provider will only be able to again take up the proceedings in which section 85 was invoked once the consumer is in default of an obligation in terms of the court-ordered re-arrangement.¹²⁶

From the discussion of section 85 and the alternative route to a possible debt review and debt rearrangement that it provides, it is apparent that the section does little more than further layering the procedural labyrinth that the NCA represents. As far as debt relief is concerned, it allows a desperate consumer, who can satisfy the court of a basket full of factors, to apply for the inclusion of debt that would have been excluded from the ambit of the debt review process. Furthermore, the fact that the court may in any proceedings take cognisance of the debtor's financial situation is a positive feature. Nevertheless, when taking a step back some of the sentiments expressed in chapter 4 are yet again relevant and have perhaps been more clearly

¹²⁴ See also s 3(c), (g) and (i).

¹²⁵ See ch 4 par 4.3.2. The Supreme Court of Appeal's stance differs from this statement as in *Collett v FirstRand Bank* 515 it remarked that a difference between the debt review procedure in terms of s 85 and that in terms of s 86 is that a credit provider cannot terminate a debt review in terms of s 85. This sentiment was later repeated by the Supreme Court of Appeal in *Seyffert v FirstRand Bank Ltd* 586–587.

¹²⁶ See Van Heerden 2013 *De Jure* 992 *et seq.*

illustrated within the ambit of section 85, namely, that the debt review process is lacking as a debt relief measure and that many problems can be eliminated by, amongst others, excluding secured credit (although special consideration as regards debtors' homes are important) from the procedure's ambit and including agreements where individual enforcement procedures have commenced.¹²⁷

5.5 Reckless credit in terms of the NCA

In *Desert Star Trading 145 (Pty) Ltd v No 11 Flamboyant Edleen CC*¹²⁸ the Supreme Court of Appeal commented that the prevention of reckless credit lending¹²⁹ is an important lodestar of the NCA. Already in its preamble the NCA refers to the objects of promotion of 'responsible credit granting and use and for that purpose to prohibit reckless credit granting'. In its objectives the NCA again emphasises the encouragement of responsible borrowing by consumers and the discouragement of reckless credit granting by credit providers.¹³⁰ The NCA discourages reckless credit extension through peremptory assessment requirements and harsh consequences where reckless credit has been extended.¹³¹ It is important to investigate the reckless credit provisions and especially the consequences that follow upon a determination that credit was recklessly granted to establish whether, and if so, to

¹²⁷ See ch 4 par 4.3.

¹²⁸ 2011 (2) SA 266 (SCA) 272.

¹²⁹ See Van Heerden 'Over-indebtedness and reckless credit' 11.4; Otto and Otto *NCA explained* 34.2; and Kelly-Louw and Stoop *Consumer credit regulation* 293–313 for discussions of reckless credit in terms of the NCA prior to the coming into effect of the Amendment Act and National Credit Regulations including Affordability Assessment Regulations GN R202 in GG 38557 of 13 March 2015, which impact on pre-agreement assessment. The latter set of regulations amended the National Credit Regulations by, amongst others, inserting reg 23A titled 'Criteria to conduct affordability assessment'. Ch 6 of the regulations provides that it is binding to the extent of its application and that non-adherence therewith will be dealt with in accordance with the remedies and procedures in terms of the NCA. See Van Heerden and Renke 2015 *Int Insolv Rev* 77 as regards the duty to conduct a pre-agreement assessment as a responsible lending practice in South Africa which takes cognisance of the Amendment Act and the regulations mentioned above. The authors remark (*ibid*) that

for the first couple of years that the Act was in operation and significantly during the global financial recess which started in 2008, the ability of the pre-agreement assessment measure to prevent reckless credit granting was stifled by the lack of guidelines on a more binding legal framework within which it had to be administered.

The article also provides insight into the build-up to the final regulations; 78–84. However, this thesis is not concerned with measures aimed at preventing over-indebtedness and information relating to the prohibition of reckless credit extension is merely provided as background to the remedies discussed later.

¹³⁰ S 3(c).

¹³¹ Van Heerden 'Over-indebtedness and reckless credit' 11.4.1.

what extent such consequences afford relief to an over-indebted or insolvent South African debtor.

Chapter 4 part D of the NCA provides for the regulation of over-indebtedness and reckless credit.¹³² Section 81, headed 'Prevention of reckless credit', ties in with the NCA's purposes in relation to reckless credit agreements (as set out in section 3) as it obliges both credit providers and consumers to conduct themselves in such a manner as to avoid the possibility of reckless credit granting and reckless credit borrowing. Consumers are required to fully and truthfully answer credit providers' requests for information as part of credit providers' assessment obligations.¹³³ This is of course to enable a credit provider to conduct a proper affordability assessment. Although it has been held that a credit provider is entitled to accept the accuracy of such information where there is no indication that would reasonably alert it to the contrary and that it is consequently not required to, as a matter of course, verify all information independently,¹³⁴ the amendment to the regulations has the effect that a credit provider is now expected (as a matter of course) to validate some information.¹³⁵ The consumer's obligation to fully and truthfully answer the credit provider's requests for information commences upon the application for credit and continues while such application is being considered.¹³⁶ Vessio notes that the wording of section 81(1) is interesting as the responsibility appears to be on the credit provider to ask the right information-gathering questions.¹³⁷ It is a complete defence to an allegation of reckless credit extension if it is established that the consumer neglected to fully and truthfully answer the credit provider's questions and a court or the Tribunal determines that such failure materially affected the credit

¹³² Reckless credit provisions have limited application; see ch 4 par 4.3.1 where the application of the NCA, with specific emphasis on ch 4 pt D, is discussed. See also reg 23A(1) and (2).

¹³³ S 81(1). See also reg 23A(6) which extends the consumer's obligations as regards reckless credit in that he must accurately disclose all financial obligations to enable the credit provider to conduct the affordability assessment. The consumer must also provide the credit provider with authentic documentation; reg 23A(7).

¹³⁴ *Horwood v FirstRand Bank Ltd* unreported case no 2010/36853 (GSJ) par 14. Date of hearing 21 September 2011.

¹³⁵ See reg 23A(3)–(4), (7), (10), (12) and (13).

¹³⁶ S 81(1). Van Heerden and Boraine 2011 *De Jure* 397 submit that during the time when the consumer's application is considered, the consumer may not apply for further credit at other credit providers without disclosing full details thereof to the credit provider who is considering the consumer's application.

¹³⁷ Vessio 2009 *TSAR* 279. See also reg 23A as regards credit providers' increased responsibilities in this respect.

provider's ability to conduct a proper assessment.¹³⁸ It is therefore not every failure by a consumer to answer questions fully and truthfully that would entitle the credit provider to the complete defence afforded by the NCA.¹³⁹

In turn, credit providers are prohibited from entering into reckless credit agreements with consumers¹⁴⁰ and are required to take reasonable steps to assess certain prescribed facts before entering into such agreements.¹⁴¹ These are the consumer's general understanding and appreciation of the risks and costs of the proposed credit and his rights and obligations under such an agreement.¹⁴² Credit providers are also required to assess a consumer's debt re-payment history relating to credit agreements entered into as a consumer¹⁴³ and the consumer's existing financial means, prospects and obligations.¹⁴⁴ There is an additional requirement where the consumer has a commercial purpose for applying for credit. In such a case the credit provider is required to assess whether there is a reasonable basis to conclude that any commercial purpose of taking up the credit may be successful.¹⁴⁵ It is thus clear that the peremptory assessment is not merely an affordability assessment. Meyer J

¹³⁸ S 81(4).

¹³⁹ *Horwood v FirstRand Bank Ltd* par 6. Van Heerden and Boraine 2011 *De Jure* 400 submit that the facts of the specific matter under consideration and the extent of the consumer's untruthfulness must be considered to determine whether the credit provider's assessment ability was materially influenced.

¹⁴⁰ S 81(3).

¹⁴¹ See Van Heerden and Boraine 2011 *De Jure* 398 where they, with reference to ss 63 and 64 of the NCA, submit that credit providers must implement non-discriminatory evaluative measures that are cast plainly and in an official language understandable to the consumer. The authors provide a list of aspects that such measures should address. See further the newly-introduced reg 23A.

¹⁴² S 81(2)(a)(i).

¹⁴³ S 81(2)(a)(ii). In *Nedbank Ltd v Soneman* 2013 (3) SA 526 (ECP) 530 the court remarked that one of the most obvious and efficient ways to determine the debt-repayment history is an enquiry into the existence of judgments previously obtained against the consumer. See further reg 23A(13) as regards debt repayment history. Also take note of s 71A which was inserted by s 22 of the Amendment Act and the Removal of Adverse Consumer Credit Information and Information Relating to Paid Up Judgements Regulations GN R144 in GG 37386 of 26 February 2014 which have a bearing on credit providers' ability to assess the whole of consumers' debt-repayment history. See also s 69 of the NCA which requires credit providers to lodge agreements with the national register of credit agreements. Van Heerden and Renke note that such a register is not yet in existence and that, at present, credit providers report the necessary information on credit agreements to credit bureaux; Van Heerden and Renke 2015 *Int Insol Rev* 87.

¹⁴⁴ S 81(2)(a)(iii). See further reg 23A(3)–(12) and specifically reg 23A(8). In exceptional cases the credit provider may accept expenses below a threshold, set out in table 1, in accordance with gross monthly income, on the completion of a questionnaire by the consumer that is set out in the schedule; reg 23A(11).

¹⁴⁵ S 81(2)(b).

in *Horwood* stated¹⁴⁶ that the correct interpretation of the above provisions is that where a credit provider has taken the required 'reasonable steps to assess' the prescribed matters, the agreement would not be reckless, irrespective of whether the assessment was spoiled by the consumer's inadequate or untruthful answers. The court was consequently of the view that the complete defence as provided for in section 81(4) is a defence which may be raised in addition to one that a credit provider's assessment obligations in terms of section 81 have been met.¹⁴⁷ Conversely, it was held in *ABSA Bank v COE Family Trust*¹⁴⁸ that section 81(4) should be read together with section 81(2). Where no assessment was undertaken by the credit provider in the first place, section 81(4) is of no relevance.¹⁴⁹

Section 80(1) the NCA provides for three types of reckless credit agreements and states that

[a] credit agreement is reckless if, at the time that the agreement was made, or at the time when the amount approved in terms of the agreement is increased, other than an increase in terms of section 119(4)¹⁵⁰ –

- (a) the credit provider failed to conduct an assessment as required by section 81(2), irrespective of what the outcome of such an assessment might have concluded at the time;¹⁵¹ or
- (b) the credit provider, having conducted an assessment as required by section 81(2), entered into the credit agreement with the consumer despite the fact that the preponderance of information available to the credit provider indicated that –
 - (i) the consumer did not generally understand or appreciate the consumer's risks, costs or obligations under the proposed credit agreement;¹⁵² or
 - (ii) entering into that credit agreement would make the consumer over-indebted.¹⁵³

¹⁴⁶ Par 7.

¹⁴⁷ *Ibid.*

¹⁴⁸ 2012 (3) SA 184 (WCC) 189.

¹⁴⁹ In light of the decision it seems that a clause in a contract indicating that a consumer understands the risks, costs, rights and obligations will not be sufficient to satisfy the court that a proper assessment was done. Evidence that the credit provider had requested information which would have ensured that the process in terms of s 81(2) was duly undertaken, is still necessary; 189. This approach is in line with the new reg 23A.

¹⁵⁰ S 119(4) is concerned with the automatic increase of a credit limit under a credit facility.

¹⁵¹ Type one reckless credit.

¹⁵² Type two reckless credit. Van Heerden 'Over-indebtedness and reckless credit' 11.4.3 n429 submits that type two reckless credit implies that the credit provider has a duty to inform the consumer of the risks, costs and obligations of the proposed credit agreement.

¹⁵³ Type three reckless credit.

When determining whether an agreement constitutes reckless credit, the person making the determination must apply the criteria above as they existed at the time that the *agreement was entered into*.¹⁵⁴ The designated person should not have regard for the ability of the consumer at the time *the determination is made* to meet the obligations under the agreement or to understand or appreciate the risks, costs and obligations under the agreement.¹⁵⁵ Thus, the fact that a consumer in the meantime became knowledgeable of the risks, costs and obligations of the agreement or can now afford such credit should not influence a determination that the agreement was recklessly entered into.¹⁵⁶

As far as the peremptory assessment is concerned, the NCA was initially not prescriptive in establishing specific criteria that credit providers had to use when conducting the assessment.¹⁵⁷ However, section 82(1) was amended by section 24 of the Amendment Act and now provides that, in addition to the requirement that a credit provider's evaluative mechanisms or models and procedures must result in a fair and objective assessment, it must not be inconsistent with the affordability assessment regulations made by the minister.¹⁵⁸ Although decided prior to the amendment of section 82, the decision in *Horwood* that the credit provider must take reasonable steps to assess the prescribed matters and that the creditor provider's evaluative mechanisms, modules and procedures must be fair and objective, is still relevant. It was also held that whether or not a credit provider has taken such

¹⁵⁴ S 80(2). See also *Horwood v FirstRand Bank Ltd* par 10.

¹⁵⁵ S 80(2). S 80(3) deals with the value of certain agreements at the time the determination is made. It provides that the value of

- (a) any credit facility is the credit limit at that time under that credit facility;
- (b) any pre-existing credit guarantee is –
 - (i) the settlement value of the credit agreement that it guarantees, if the guarantor has been called upon to honour that guarantee; or
 - (ii) the settlement value of the credit agreement that it guarantees, discounted by a prescribed factor; and
- (c) any new credit guarantee is the settlement value of the credit agreement that it guarantees, discounted by a prescribed factor.

See further reg 23A.

¹⁵⁶ Van Heerden 'Over-indebtedness and reckless credit' 11.4.4.

¹⁵⁷ See the quote by Van Heerden and Renke *Int Insolv Rev 77* as referred to above.

¹⁵⁸ See also s 61(5) which provides that

[a] credit provider may determine for itself any scoring or other evaluative mechanism or model to be used in managing, underwriting and pricing credit risk, provided that any such mechanism or model is not founded or structured upon a statistical or other analysis in which the basis of risk categorisation, differentiation or assessment is a ground of unfair discrimination prohibited in section 9(3) of the Constitution.

reasonable steps to meet its assessment obligations is to be determined objectively and on the facts and circumstances of each case.¹⁵⁹ However, in the realm of a credit provider's assessment obligation, Levenberg J in *SA Taxi Securitisation v Mbatha*¹⁶⁰ remarked that although one of the purposes of the NCA is to discourage reckless credit, the NCA is also designed to facilitate access to credit to those who were previously denied such access. An overcritical armchair approach by the courts towards reckless credit extension or excessive penalties where such lending has occurred would, according to the court, significantly chill the availability of credit, especially to the less affluent consumers.

The amendment of section 82(1) was referred to above. Section 82(1) and (2), after its amendment, provides as follows:¹⁶¹

- (1) A credit provider may determine for itself the evaluative mechanisms or models and procedures to be used in meeting its assessment obligations under section 81, provided that any such mechanism, model or procedure results in a fair and objective assessment and must not be inconsistent with the affordability assessment regulations made by the Minister.
- (2) The Minister must, on recommendation of the National Credit Regulator, make affordability assessment regulations.¹⁶²

Subsequent to this amendment the minister promulgated affordability assessment regulations¹⁶³ on 13 March 2015.¹⁶⁴ Van Heerden and Renke¹⁶⁵ submit that the effect of the amendment is that a credit provider's evaluative mechanisms or modules and procedures as a minimum requirement must now be aligned with the affordability assessment regulations.

As was previously stated, the possible consequences of reckless credit and more specifically the question whether such consequences could result in any form of debt relief where a consumer is already over-committed is of particular importance for purposes of this thesis. Section 83 details these consequences. The original heading of the section, namely, 'Court may suspend reckless credit agreement' has been

¹⁵⁹ *Horwood v FirstRand Bank Ltd* par 5.

¹⁶⁰ 2011 (1) SA 310 (GSJ) 317.

¹⁶¹ S 24(a) of the Amendment Act.

¹⁶² See the newly introduced reg 23A.

¹⁶³ Reg 23A and definitions to give effect to reg 23A.

¹⁶⁴ See GN R 202 GG 38557 of 13 March 2015.

¹⁶⁵ Van Heerden and Renke 2015 *Int Insolv Rev* 83.

substituted with 'Declaration of reckless credit agreement' by section 25 of the Amendment Act. It is important to note that section 83 has in the past only referred to 'court', but has been amended to also extend the powers in terms of reckless credit agreements to the Tribunal. The section firstly provides that, despite any provision of law or agreement to the contrary, in any court or Tribunal proceedings where a credit agreement is being considered, the court, or Tribunal as the case may be, may declare the agreement to be reckless in accordance with chapter 4 part D.¹⁶⁶ The section continues by setting out the orders that a court or the Tribunal *may* make, depending on the type of reckless credit that was extended. However, section 83 should be read together with section 130(4)(a) which provides that in any proceedings contemplated in the said section and where a court has determined that an agreement was reckless as described in section 80 the court *must* make an order as contemplated in section 83.¹⁶⁷ The court or the Tribunal therefore has no discretion and is required to make the appropriate order(s) in terms of section 83 once it has determined that reckless lending has occurred.

Even though the first two types of reckless credit are not primarily concerned with the situation where the consumer is over-indebted, it may also find application in such instances and are therefore discussed here. Reckless credit type one takes place when no credit assessment as required by section 81(2) was conducted and reckless credit type two when an assessment was conducted but the consumer did not generally understand or appreciate the risks, costs or obligations relating to the agreement. Where one of these types of reckless credit has been established, section 83(2) provides that the court or Tribunal may make an order

- (a) setting aside all or part of the consumer's rights and obligations under that agreement, as the court¹⁶⁸ determines just and reasonable in the circumstances; or

¹⁶⁶ S 83(1). Van Heerden and Boraine 2011 *De Jure* 400–401 note that the court may, in contrast to its powers in terms of s 85, *suo motu* take cognisance of the reckless credit provisions and that both action and application proceedings are included in the phrase 'court proceedings'. The article was written prior to the amendment that resulted in a referral to the Tribunal. See further *African Bank Ltd v Myambo* 2010 (6) SA 298 (GNP) and *Ford*. See also the discussion of *Ford* in ch 3 par 3.3.2.3.

¹⁶⁷ S 130(4)(a) has not been amended and in this regard only refers to 'court'. It is submitted that the omission is an oversight.

¹⁶⁸ It is submitted that the fact that s 83(2)(a) has not been amended to also refer to the Tribunal is a mere omission.

- (b) suspending the force and effect of that credit agreement in accordance with subsection (3)(b)(i).

Even though there is no provision detailing the setting aside of an agreement and the effects of such an order, the suspension of the order and its consequences are regulated by section 84. The latter provides that while the force and effect of an agreement is suspended, the consumer is not required to make any payment under the agreement;¹⁶⁹ no interest, fee or other charge may be charged to the consumer;¹⁷⁰ and the credit provider's rights under the agreement or any law in respect thereof are unenforceable, despite any law to the contrary.¹⁷¹ Section 84(2) provides that after the suspension of the force and effect of the agreement has come to an end all respective rights and obligations of both the credit provider and the consumer in terms of the agreement revive and are fully enforceable except to the extent that a court (and presumably the Tribunal) may otherwise order.¹⁷²

Van Heerden and Boraine note that, when analysing section 83(2), the NCA is silent on how a court should decide between setting aside and suspension orders. They further note that the NCA does not differentiate between situations where performance has not yet occurred and where the parties have already performed. The NCA fails to indicate what the rights and obligations of a credit provider are where the consumer's rights and obligations are set aside whether partially or completely. The NCA does not indicate on what basis it will be 'just and reasonable in the circumstances' to completely set aside rights and obligations. Although Van Heerden and Boraine submit that the absence of clear guidelines regarding setting aside orders and the absence of an indication by the legislature as to when the setting aside of obligations will be more appropriate than suspension could lead to a fragmented approach by the courts and that such uncertainty requires clarification,¹⁷³ the Amendment Act does not provide more detail in this regard.

¹⁶⁹ S 84(1)(a).

¹⁷⁰ S 84(1)(b). S 84(2)(b) provides that for greater certainty, no amount may be charged by the credit provider to the consumer in respect of any interest, fee or other charge that such credit provider was unable to charge during the suspension of the agreement.

¹⁷¹ S 84(1)(c). Once again, the subsection should have referred to the Tribunal as well. The omission is probably an oversight.

¹⁷² S 84(2)(a).

¹⁷³ Van Heerden and Boraine 2011 *De Jure* 402–403.

Van Heerden and Boraine submit that the choice of suspension rather than the setting aside of an agreement should be influenced by the question whether the lack of an affordability assessment or of comprehension of the risks, costs or obligations by the consumer *subsequently* led to the consumer's over-indebtedness where the consumer requires a 'debt-breather' to recover. According to them this scenario should be distinguished from the situation in section 80(1)(b)(ii), discussed hereinafter, where the agreement caused over-indebtedness at the moment it was entered into. The crux of their argument is that the suspension remedy seems to be designed with temporary relief, aimed at the alleviation of over-indebtedness, in mind and does not serve as an arbitrary measure to merely punish a credit provider. The authors further submit that where the facts of a case indicate that a consumer will not recover financially despite a suspension, it will serve no purpose to make such an order.¹⁷⁴ They note that in instances where the agreement is suspended a credit provider's 'punishment' for extending reckless credit is that it will not receive payment during such time, may not charge interest, fees or other charges to the consumer and is not allowed to enforce the agreement. However, the legislature did not clarify what would happen to securities that form the subject of such suspended agreements.¹⁷⁵

In *Mbatha* Levenberg J had to decide, amongst others, on the court's powers and the intention of the legislature as regards a suspension as contemplated in section 84. The court found it significant that the said section focuses on whether the consumer is required to make payments or pay interest, fees or other charges during the suspension period. It stated that although section 84(1)(c) provides that a credit provider will not be entitled to enforce its rights during the suspension period, the prohibition should be read with subsections 84(1)(a) and (b) in mind. The court consequently held that there is no basis for reading in a provision that the courts hold the power to permit the consumer to utilise the security during the period of suspension in such a manner that will allow its deterioration.¹⁷⁶ The court went further and stated that it doubted whether the legislature ever intended that the consumer should keep the 'money and the box'. Where the consumer obtained

¹⁷⁴ *Idem* 404.

¹⁷⁵ *Idem* 405–406.

¹⁷⁶ *SA Taxi Securitisation (Pty) Ltd v Mbatha* 319.

possession and use of the goods where no credit should have been extended in the first place, it would be ‘fundamentally unfair and counterproductive’ to allow the consumer the continued use of the goods whilst not effecting payments in terms of the agreement.¹⁷⁷ The court held that the effect of suspension, as opposed to the setting aside of all or part of the consumer’s obligations, is that all elements of the credit agreement would be suspended. This would mean that the consumer is not entitled to continued possession of the goods during the time of suspension.¹⁷⁸ The consumer conversely does not have to make payments during the said period.¹⁷⁹

However, if *Mbatha* is correct in that the consumer may not keep the ‘money and the box’, the practical question remains as to what should physically happen to the object of security. In this regard Van Heerden and Borraine submit, in the realm of movable property, that although the credit provider will not be entitled to cancellation of the credit agreement and to repossession of the goods, he may apply for an interim attachment order for safekeeping where the credit provider will suffer irreparable harm due to depreciation while the object remains in possession of the consumer.¹⁸⁰ However, the writers foresee various difficulties regarding the situation where the object of security is immovable property.¹⁸¹

From a debt-relief perspective, the only benefit that a suspension order could possibly offer an over-indebted consumer over and above a section 87 re-arrangement in terms of the debt review procedure is that the relevant credit provider may not charge interest, fees or other charges to the consumer during the period for which the suspension subsists.¹⁸² However, holistically viewed and as is the case

¹⁷⁷ *Ibid.* See also 320.

¹⁷⁸ Corroboration for this point is according to Van Heerden and Borraine found in s 84(2) which provides that all the rights and obligations of both the consumer and the credit provider would be revived and are fully enforceable after the suspension has come to an end. The section thus assumes that suspension not only has an effect on the rights of the credit provider, but also on that of the consumer; Borraine and Van Heerden 2011 *De Jure* 406.

¹⁷⁹ At 319.

¹⁸⁰ See also *SA Taxi Securitisation (Pty) Ltd v Chesane* 2010 (6) SA 557 (GSJ) as regards the NCA’s silence relating to the interim attachment of goods in general.

¹⁸¹ Van Heerden and Borraine 2011 *De Jure* 407–408.

¹⁸² See s 87 read together with s 86(7)(c)(ii)(bb) and (cc) as regards debt re-arrangements and cf s 84.

with the debt review procedure, a suspension order will only assist mildly over-indebted individuals as it does not result in the discharge of debt.¹⁸³

As far as the setting aside of a credit agreement is concerned, it was held in *Mbatha* that where the consumer has a valid complaint that if it was not for the recklessness of the credit provider, the consumer would never have entered into the agreement, it might be 'just and reasonable' to 'set aside' the agreement. The effect of the setting aside of the consumer's rights and obligations where the parties have already performed in terms of the agreement would result in the agreement being null and void.¹⁸⁴ The credit provider who remained the owner of for instance a vehicle, would therefore be entitled to restoration.¹⁸⁵ In turn, the consumer has no obligations under the agreement and would be relieved of further indebtedness or a deficiency claim.¹⁸⁶ Van Heerden and Borraine propose that where the consumer's rights and obligations are set aside under circumstances where performance has not yet occurred it might be just and reasonable to order that the consumer has no further rights and obligations which will effectively amount to a cancellation of the agreement. As a result both parties are absolved from reciprocal performance.¹⁸⁷ From a debt relief perspective, the setting aside of an agreement offers an insolvent debtor significant benefits as such an order effectively brings an end to the consumer's obligations in terms of the agreement. In other words, the consumer is relieved from future indebtedness.¹⁸⁸ Such a release is not competent in terms of a section 87 re-arrangement order as the NCA generally requires the satisfaction of all obligations.¹⁸⁹

It seems that the manner in which a court (or the Tribunal) should decide between the setting aside or suspension orders remains a contentious issue. However, it is submitted that, as section 130(4)(a) is cast in peremptory terms, these orders were

¹⁸³ See ch 4 par 4.3.5.

¹⁸⁴ 319.

¹⁸⁵ See also *SA Taxi Securitisation (Pty) Ltd v Chesane* 563. Borraine and Van Heerden 2010 *THRHR* 656 state that section 83(2)(a) does not oust other possible causes of action such as unjustified enrichment.

¹⁸⁶ *SA Taxi Securitisation (Pty) Ltd v Mbatha* 319.

¹⁸⁷ Borraine and Van Heerden 2010 *THRHR* 653.

¹⁸⁸ See Van Heerden and Borraine 2011 *De Jure* 403–404.

¹⁸⁹ See ch 4 para 4.3.2 and 4.3.5. See also s 3(g).

designed to facilitate compulsory assistance or reward to a debtor to whom reckless credit has been extended, and to ‘discipline’ the credit provider who extended such credit.

Section 83(3) deals with the orders that the court or Tribunal may make in case of the third type of reckless credit provision, namely, where entering into the credit agreement caused the consumer’s over-indebtedness. In such a case the court or Tribunal

- (a) must further consider whether the consumer is over-indebted at the time of those proceedings; and
- (b) if the court or Tribunal, as the case may be, concludes that the consumer is over-indebted, the said court or Tribunal may make an order –
 - (i) suspending the force and effect of that credit agreement until a date determined by the Court when making the order of suspension; and
 - (ii) restructuring the consumer’s obligations under any other credit agreements, in accordance with section 87.¹⁹⁰

Section 83(4) requires the court or the Tribunal to consider two aspects before making an order as contemplated in subsection (3). These are the consumer’s current means and ability to pay its current financial obligations as they existed at the time the agreement was made¹⁹¹ and the expected date when any such obligation will be fully satisfied, assuming that all required payments in accordance with any proposed order are made.¹⁹²

It is apparent that with the third type of reckless credit, the consumer’s over-indebtedness at both the time the agreement was entered into and as at the time the determination of reckless credit is made, is relevant.¹⁹³ Where an agreement resulted in the consumer’s over-indebtedness and, provided that the consumer is still over-indebted at the time of the proceedings, the court or Tribunal is entitled to suspend the force and effect of the agreement under consideration and to restructure the consumer’s obligations under other credit agreements. An order

¹⁹⁰ S 87 deals with the re-arrangement of a consumer’s obligations by a magistrate’s court. See ch 4 par 4.3.2 in this regard.

¹⁹¹ S 83(4)(a).

¹⁹² S 83(4)(b). The latter aspect indicates the importance of such information in devising an appropriate period for the suspension of an agreement; Van Heerden ‘Over-indebtedness and reckless credit’ 11.4.5.2.

¹⁹³ *Ibid.*

setting aside the consumer's obligations is therefore not competent when *only* the third type of reckless credit is pertinent. However, it is submitted that more than one type of reckless credit extension may exist in respect of a particular set of facts and that a setting aside order could be a possibility where a consumer is found to be over-indebted as a result of reckless credit granting.

Where the third type of reckless credit occurs, a credit provider, in addition to the adverse consequences as provided for in section 84, will also suffer the embarrassment that other credit providers will be treated preferentially when a restructuring of the consumer's obligations is ordered.¹⁹⁴ The effect of a restructuring of obligations on the consumer's financial situation was dealt with extensively in chapter 4¹⁹⁵ where it was established that it only results in limited relief.¹⁹⁶

As a last consideration, *Mbatha* provided a non-exhaustive list of guidelines that will assist the consumer in demonstrating that reckless credit was extended.¹⁹⁷ The onus to prove that credit was granted recklessly thus generally rests on the consumer.¹⁹⁸

5.6 Other measures in terms of the NCA

5.6.1 Surrender of goods

A consumer may voluntarily surrender¹⁹⁹ goods forming the subject of an instalment agreement, secured loan or a lease and the NCA prescribes a specific procedure that a credit provider must follow subsequent to such surrender.²⁰⁰ This procedure is provided for in section 127 of the NCA²⁰¹ and is referred to as an extraordinary right.²⁰² The procedure is structured to rid consumers of certain credit agreements,²⁰³ but does not result in any discharge of debt *per se*.

¹⁹⁴ See Van Heerden and Boraine 2011 *De Jure* 409.

¹⁹⁵ See ch 4 para 4.3.2 and 4.3.5.

¹⁹⁶ See ch 4 par 4.3 in general.

¹⁹⁷ At 321.

¹⁹⁸ Van Heerden 'Over-indebtedness and reckless credit' 11.4.5.

¹⁹⁹ This section on the consumer's right to surrender goods is based on Coetzee *Impact 122 et seq.*

²⁰⁰ Only instalment agreements, secured loans and leases are referred to even though the NCA applies to a wider scope of agreements as discussed in ch 4 par 4.3.1.

²⁰¹ See Otto 'Conclusion, alteration and termination of credit agreements' 9.5.4; Otto and Otto *NCA explained* 30.12; Kelly-Louw and Stoop *Consumer credit regulation* 282 *et seq* and Coetzee 2010 *THRHR* 569 for discussions of the s 127 procedure.

²⁰² See Otto 'Conclusion, alteration and termination of credit agreements' 9.5.4.1.

²⁰³ *Ibid.*

The consumer sets the process in motion by delivering a written notice to the credit provider to terminate the agreement.²⁰⁴ If the goods that are subject to the instalment agreement, secured loan or lease are in the credit provider's possession, the consumer merely requests the credit provider to sell the goods.²⁰⁵ If the goods are not in the possession of the credit provider, the consumer must return them to the credit provider within five business days after the date of the notice, unless otherwise agreed between the parties.²⁰⁶

Within ten business days after the later of receipt of the notice²⁰⁷ or receiving the goods from the consumer,²⁰⁸ the credit provider must furnish the consumer with a written notice indicating the estimated value of the goods.²⁰⁹ A non-defaulting consumer then has ten business days²¹⁰ to withdraw the notice of termination unconditionally and resume possession of the goods.²¹¹ A consumer in default of the credit agreement is not entitled to withdraw the termination notice.²¹²

The credit provider must return the goods to a non-defaulting consumer who has elected to exercise the right of withdrawal of the earlier termination notice.²¹³ If the consumer is in default or where a non-defaulting consumer has not responded to the valuation notice, the credit provider must sell the goods as soon as possible for the best price reasonably obtainable.²¹⁴

After the sale of the goods, the credit provider must credit the consumer's account with the proceeds of the sale less reasonable expenses in connection with the sale, or debit the consumer's account with a charge.²¹⁵ The credit provider must further

²⁰⁴ S 127(1)(a).

²⁰⁵ S 127(1)(b)(i).

²⁰⁶ S 127(1)(b)(ii). Goods must be returned to the credit provider's place of business during ordinary business hours.

²⁰⁷ S 127(1)(b)(i).

²⁰⁸ S 127(1)(b)(ii).

²⁰⁹ S 127(2).

²¹⁰ After receiving the notice as contemplated in s 127(2).

²¹¹ S 127(3).

²¹² *Ibid.*

²¹³ S 127(4)(a).

²¹⁴ S 127(4)(b).

²¹⁵ S 125(5)(a). The consumer's account will be debited where the proceeds of the sale could not entirely extinguish the costs of the sale; see Otto 'Conclusion, alteration and termination of credit agreements' 9.5.4.4.

furnish a notice to the consumer setting out the settlement value prior to the sale,²¹⁶ the gross amount realised,²¹⁷ the net proceeds of the sale,²¹⁸ and the amount credited or debited to the consumer's account.²¹⁹ If the amount credited to the consumer's account is less than the settlement value or an amount is debited to the account, the credit provider may further demand payment of the outstanding balance in the notice.²²⁰ If a surplus remains after crediting the consumer's account and another credit provider has a registered agreement in respect of the same goods, the excess amount must be remitted to the Tribunal which may order the distribution of this amount in a just and reasonable manner.²²¹ If no other credit provider has a registered agreement relating to the same goods, the balance must be remitted to the consumer when delivering the notice in terms of section 127(5)(b) and the agreement is terminated upon such remittance.²²²

As was mentioned, if a shortfall remains after an amount was credited to the consumer's account or when an amount was debited to the consumer's account, the credit provider may demand payment of the outstanding amount when issuing the section 127(5)(b) notice.²²³ In the event that the consumer fails to settle the outstanding amount within ten business days from receiving the notice,²²⁴ the credit provider may commence with enforcement proceedings in terms of the Magistrates' Courts Act.²²⁵ If the demanded is paid at any time before judgment is obtained, the agreement is terminated upon payment.²²⁶

²¹⁶ S 127(5)(b)(i).

²¹⁷ S 127(5)(b)(ii).

²¹⁸ S 127(5)(b)(iii).

²¹⁹ S 127(5)(b)(iv).

²²⁰ S 127(5) read together with s 127(7).

²²¹ S 127(6)(a).

²²² S 127(6)(b).

²²³ S 127(7). It is clear that the s 127(7) notice is a prerequisite for enforcement of the remaining obligations under the agreement. Boraine and Renke submit that a s 129(1)(a) notice need not be sent where the credit provider approaches a court for an order enforcing remaining obligations following a voluntary surrender in terms of s 127; Boraine and Renke 2008 *De Jure* 6 n160. Van Heerden 'Enforcement of credit agreements' 12.8.3.1 holds the opposite view.

²²⁴ The fact that receipt of the notice is required will inevitably lead to evidential problems; see Van Heerden and Otto 2007 *TSAR* 658 n34.

²²⁵ S 127(8)(a). The credit provider may still approach the high court in this regard as its jurisdiction is not ousted by s 127(8). See *Nedbank Ltd v Mateman*; *Nedbank Ltd Stringer* 2008 (4) SA 276 (T). See also Van Heerden 2008 *TSAR* 840 and Roestoff and Coetzee 2008 *THRHR* 678 regarding the jurisdiction of the courts in relation to matters governed by the NCA.

²²⁶ S 127(8)(b).

Interest is payable on the outstanding amount at the rate applicable to the credit agreement, as from the time of the demand until the outstanding balance has been fully settled.²²⁷ A credit provider who fails to follow the procedure as set out in section 127 is guilty of an offence.²²⁸

Section 127 thus bestows a statutory right on a consumer to unilaterally terminate an instalment agreement, a secured loan or a lease by voluntarily surrendering goods forming the subject of such agreements to the credit provider concerned. The voluntary surrender of property is initiated by the consumer giving notice to terminate the agreement and surrendering the goods to the credit provider where after the credit provider is obliged to meticulously follow the prescribed procedure contained in section 127.

A critical issue that must be addressed is what exactly the legislature had in mind with the phrase 'goods that are the subject of that agreement' in section 127(1)(b)(ii). The meaning of the word 'goods' and the meaning thereof within the quoted phrase must be considered. As 'goods' are neither defined in the NCA nor the regulations it is submitted that it should bear its ordinary meaning, being a reference to movable property.²²⁹ This inference is strengthened by the usage of the word within its context as the section only applies to instalment agreements, secured loans and leases all of which concern movable property only.²³⁰

The phrase 'goods that are the subject of that agreement' encompasses two situations, namely (a) where movable goods are financed under a credit agreement²³¹ irrespective of whether ownership passed or had been retained,²³² and (b) where movable goods are used as security for payment of amounts due under a credit agreement.²³³

²²⁷ S 127(9). It seems that by implication a credit provider's right to interest is suspended prior to such demand.

²²⁸ S 127(10).

²²⁹ A brief but workable definition of 'goods' is that of Milne *et al Bell's*, viz that 'Goods shall mean goods, luggage or other movable property of any description'.

²³⁰ See ch 4 par 4.3.1 for definitions of the agreements.

²³¹ In the case of an instalment agreement or a lease.

²³² Ownership can either pass or be retained under an instalment agreement.

²³³ In the case of a secured loan.

It should be noted that section 127(3) provides a specific statutory right to the consumer who provided a notice of termination to withdraw such notice and resume possession of any goods surrendered to the credit provider. The requirements to exercise this right are that the consumer must have received a valuation notice and that he must not be in default under the credit agreement. This right must be exercised within ten business days after the consumer has received the valuation notice.

The words ‘unless the consumer *is* in default’²³⁴ in section 127(3) do not mean that the consumer was *never* in default. Section 127(3) could well be interpreted that if a consumer was in default, the default was remedied in that the consumer brought payments up to date and has thereby cancelled the default. However, it is clear that a consumer may not withdraw the notice of termination whilst in default. The agreement is not terminated upon the provision of the consumer’s written notice of termination as sections 127(6)(b) and 127(8)(b) clearly provide that the agreement is only terminated upon remittance of a surplus amount to the consumer in the case where section 127(6)(b) is applicable, or when the consumer remits the shortfall to the credit provider in circumstances to which section 127(8)(b) applies.

Section 127 has improved the situation of debtors by providing a statutory right to unilaterally terminate an instalment agreement, a secured loan or a lease. It is submitted that this provision is especially useful in dealing with an insolvent debtor’s situation as it can be used to rid the debtor of some of his excess debt before resorting to the primary²³⁵ or one of the secondary²³⁶ debt relief procedures. It will further demonstrate good faith on the consumer’s part in attempting to remedy his situation as far as possible. The situation of consumers has further been improved in that the section provides that if a consumer did not withdraw the notice of termination or when the consumer is still in default after the ten-day period has lapsed, a credit provider must sell the surrendered property as soon as practicable for the best price reasonably obtainable. Whether a credit provider has complied with the direction that goods must be sold ‘as soon as practicable for the best price reasonably obtainable’,

²³⁴ My emphasis.

²³⁵ See ch 3 par 3.3.

²³⁶ See ch 4.

will depend on, amongst others, the type of goods, market conditions, the condition of the goods and customs and practice in the specific industry.²³⁷ Even though consumers must still settle any shortfall, credit providers may clearly not sell the goods for just any price.²³⁸

Another provision that is relevant to circumstances where the consumer has chosen to make use of his section 127 right is section 128 which deals with a disputed sale of goods. In terms of section 128,²³⁹ the Tribunal may review a disputed sale of goods in terms of section 127 if the consumer could not resolve the dispute directly or through alternative dispute resolution with the credit provider. The Tribunal may order the credit provider to pay the consumer an amount exceeding the net proceeds of the sale if the Tribunal is not satisfied that the goods have been sold as soon as practical for the best reasonably obtainable price. Such a decision by the Tribunal is subject to appeal or review by the high court to the extent permitted by section 148.

5.6.2 Cooling-off right

Section 121 provides a consumer with a cooling-off right under certain circumstances.²⁴⁰ A consumer may terminate a lease or an instalment agreement²⁴¹ entered into at a location other than the credit provider's registered place of business²⁴² within five business days after he has signed the agreement.²⁴³ Such termination is effected upon the delivery of a prescribed notice to the credit provider²⁴⁴ whilst tendering the return of money or goods or paying in full for services received in respect of the agreement.²⁴⁵

²³⁷ Van Heerden and Otto 2007 *TSAR* 657 n28.

²³⁸ Campbell and Logan *The credit guide* 112.

²³⁹ See Otto 'Conclusion, alteration and termination of credit agreements' 9.5.4.5; Otto and Otto *NCA explained* 30.12; and Kelly-Louw and Stoop *Consumer credit regulation* 285 *et seq* as regards s 128. See the latter source as regards applications lodged at the Tribunal in terms of s 128.

²⁴⁰ See in general Otto 'Conclusion, alteration and termination of credit agreements' 9.5.2; Otto and Otto *NCA explained* 30.10 and Kelly-Louw and Stoop *Consumer credit regulation* 223–224.

²⁴¹ See ch 4 par 4.3.1 as regards the application of the NCA in general and definitions of the various agreements.

²⁴² S 121(1).

²⁴³ S 121(2).

²⁴⁴ S 121(2)(a).

²⁴⁵ S 121(2)(b).

The credit provider must within seven business days after delivery of the notice of termination refund any money that the consumer has paid in terms of the agreement.²⁴⁶ He may also require the consumer to pay²⁴⁷

- (i) the reasonable cost of having any goods returned to the credit provider and restored to saleable condition; and
- (ii) a reasonable rent for the use of those goods for the time that the goods were in the consumer's possession, unless those goods are in their original packaging and it is apparent that they have remained unused.

Where a credit provider has unsuccessfully attempted, directly and through alternative dispute resolution,²⁴⁸ to resolve a dispute over the depreciation of property that was returned in terms of section 121, he may apply to the court for relief.²⁴⁹ In the event that a court determines that the actual fair market value of the goods has depreciated while in the consumer's possession it may order the consumer to pay an amount to the credit provider. However, such amount may not be more than the difference between the actual depreciation in fair market value and the amount that the credit provider is entitled to charge the consumer in terms of subsection (3)(b).²⁵⁰

The cooling-off right ultimately leads to the termination of an agreement and is therefore valuable in relieving the consumer from future indebtedness. However, as is apparent from its discussion, the cooling-off right will only apply in very limited instances and would therefore not regularly be available to insolvent consumers.

5.6.3 Early settlement rights

Section 125 provides that 'a consumer or guarantor is entitled to settle the credit agreement at any time'.²⁵¹ This may take place with or without the consumer giving the credit provider advance notice.²⁵²

²⁴⁶ S 121(3)(a).

²⁴⁷ S 121(3)(b).

²⁴⁸ In terms of ch 4 pt A.

²⁴⁹ S 121(4).

²⁵⁰ S 121(5).

²⁵¹ See Otto 'Conclusion, alteration and termination of credit agreements' 9.5.3.2; Otto and Otto *NCA explained* 30.11 and Kelly-Louw and Stoop *Consumer credit regulation* 280–281 for discussions of early settlement rights.

²⁵² S 125(1).

The NCA prescribes the manner in which the settlement amount should be calculated. This amount includes the unpaid balances of the principal debt, interest, other fees and charges at the time.²⁵³ Where the agreement qualifies as a large agreement the following amounts may be included:²⁵⁴

- (i) at a fixed rate of interest, an early termination charge no more than a prescribed charge or, if no charge has been prescribed, a charge calculated in accordance with subparagraph (ii); or
- (ii) other than a fixed rate interest, an early termination charge equal to no more than the interest that would have been payable under the agreement for a period equal to the difference between –
 - (aa) three months; and
 - (bb) the period of notice of settlement if any, given by the consumer.

A consumer may also at any time and without notice or penalty prepay an amount owed in terms of a credit agreement.²⁵⁵ A credit provider must accept payment so tendered²⁵⁶ and must, on the date of receipt of payment, credit payments in the following manner:²⁵⁷

- (a) Firstly, to satisfy any due or unpaid interest charges;
- (b) secondly, to satisfy any due or unpaid fees or charges; and
- (c) thirdly, to reduce the amount of the principal debt.

The invocation of consumers' early settlement rights may lead to the termination of credit agreements and could therefore relieve consumers from future indebtedness. However, these provisions will not regularly suit insolvent circumstances as financially overcommitted individuals by definition do not have surplus funds to devote to such payments. Nevertheless, it is submitted that, depending on the circumstances of a particular case, these rights could be used in tandem with consolidation agreements²⁵⁸ to assist insolvent debtors.

²⁵³ S 125(2)(a) and (b).

²⁵⁴ S 125(2)(c).

²⁵⁵ S 126(1).

²⁵⁶ S 126(2).

²⁵⁷ S 126(3).

²⁵⁸ The Act does not define 'consolidation agreement'. However, Renke provides the following definition: 'an agreement in terms whereof a consumer's existing debt is consolidated under one agreement'; Renke *An evaluation* 461 n407. Reckless credit provisions do not find application to consolidation agreements; see par 5.5. However, depending on the circumstances, where not all debts are consolidated in this manner, those that are settled may be set aside as voidable preferences; see s 29(1) of the Insolvency Act.

5.7 Common law composition

A composition in the context of insolvency law can be defined as²⁵⁹

an agreement between the insolvent and his or her creditors in terms of which the parties agree that the creditors' claims will be paid partially or in full, subject to certain circumstances and conditions, as a full and final settlement.

In South African insolvency law, a composition can be reached by making use of the statutory procedure in terms of section 119 of the Insolvency Act, as discussed in chapter 3,²⁶⁰ or a debtor may agree to a composition in terms of the common law.²⁶¹ A common law composition is usually attempted once a provisional sequestration order was granted.²⁶² Such a composition is based on the principles of the law of contract and therefore, unlike the statutory procedure, the common law composition will only bind those creditors who agreed to it.²⁶³ Consequently and for practical reasons, negotiating debt relief by making use of this common law instrument will only be useful if it is accepted by all creditors.²⁶⁴ Where the composition's formation is conditional upon all or some of the creditors agreeing to it, no creditor shall be bound until the condition is fulfilled.²⁶⁵ The common law composition has the benefits of not affecting the status of the debtor or his contractual capacity and that his assets remain vested in him.²⁶⁶ Some of the manifestations of the common law composition are the conclusion of a new contract of release,²⁶⁷ compromise²⁶⁸ or novation²⁶⁹

²⁵⁹ Boraine and Delpont 'Insolvency' 570.

²⁶⁰ Par 3.4.

²⁶¹ See Bertelsmann *et al Mars* 547; Roestoff 'n *Kritiese evaluasie* 422 *et seq*; and Smith 1968 *THRHR* 29.

²⁶² See Meskin *Insolvency law* 13.2 and Roestoff 'n *Kritiese evaluasie* 422. The statutory composition can only be utilised after the first meeting of creditors which takes place after a final order was made; see ch 3 par 3.4.

²⁶³ See *De Wit v Boathavens CC* 1989 (1) SA 606 (C) 611.

²⁶⁴ See Roestoff 'n *Kritiese evaluasie* 422–423.

²⁶⁵ See Meskin *et al Insolvency law* 13.2 and authorities cited there.

²⁶⁶ Smith 1968 *THRHR* 29–30.

²⁶⁷ Release can be described as a bilateral act based on consensus between the two contracting parties where the creditor makes an offer to release the debtor and where the debtor may accept such an offer or not. A debtor commits an act of insolvency in terms of s 8(e) of the Insolvency Act where he makes or attempts to make an arrangement with his creditors to release him from his debt; Otto and Prozesky-Kuschke 'Breach of contract and termination of contractual relationship' 148.

²⁶⁸ A compromise or settlement refers to an agreement between parties to settle a dispute. Where a dispute is settled in such a manner, the original contract is terminated and substituted by a new settlement contract which will from there on regulate the rights and duties of the parties; Otto and Prozesky-Kuschke 'Breach of contract and termination of contractual relationship' 148–149.

²⁶⁹ Novation refers to the situation where parties to a valid contract conclude a second contract with the intention of terminating and substituting the original contract therewith. An old debt is

Footnote continues on next page

which would have the effect of terminating the original contract.²⁷⁰ In some instances such a termination may afford debt relief to an over-committed consumer in that debt is written off in whole or in part or in that the terms of repayment are rendered more favourable in subsequent contracts. However, as these contracts merely represent different forms of the common law composition without any statutory recognition, Roestoff points out that the conclusion thereof will only provide a solution to a debtor whose creditors are willing to conclude such agreements.²⁷¹

As has been noted in chapter 4,²⁷² although Boraine *et al* are of the view that the administration order and debt review procedures may be applied simultaneously, they propose that debts that are excluded from the debt review procedure should rather be dealt with by supplementing the debt review procedure with voluntary compositions.²⁷³

5.8 Extinctive prescription

Extinctive (or strong) prescription of contractual debts through lapse of time²⁷⁴ is the last ancillary debt relief measure discussed in this chapter. This measure has, in contrast with most ancillary procedures discussed above, real debt relief as a consequence as it extinguishes debt.²⁷⁵ However, the Prescription Act²⁷⁶ was not

therefore extinguished through the creation of a new debt in its place; Otto and Prozesky-Kuschke 'Breach of contract and termination of contractual relationship' 149.

²⁷⁰ Otto and Prozesky-Kuschke 'Breach of contract and termination of contractual relationship' 148.

²⁷¹ Roestoff *'n Kritiese evaluasie* 420.

²⁷² Par 4.3.4.

²⁷³ See Boraine *et al* 2012 *De Jure* 267.

²⁷⁴ S 11 of the Prescription Act sets out the following periods of prescription:

- (a) thirty years in respect of –
 - (i) any debt secured by a mortgage bond;
 - (ii) any judgment debt;
 - (iii) any debt in respect of any taxation imposed or levied by or under any law;
 - (iv) any debt owed to the State in respect of any share of the profits, royalties or any similar consideration payable in respect of the right to mine minerals or other substances;
- (b) fifteen years in respect of any debt owed to the State and arising out of an advance or loan of money or sale or lease of land by the State to the debtor unless a longer period applies in respect of the debt in question in terms of paragraph (a);
- (c) six years in respect of a debt arising from a bill of exchange or other negotiable instrument or from a notarial contact, unless a longer period applies in respect of the debt in question in terms of paragraph (a) or (b);
- (d) save where an Act of Parliament provides otherwise, three years in respect of any other debt.

²⁷⁵ See Hutchison and Pretorius *The law of contract* 387.

²⁷⁶ Ch III of the Prescription Act deals with prescription of debts.

designed with debt relief in mind, but rather 'to promote certainty in the affairs of people and is aimed at fairness towards a debtor'.²⁷⁷ Prescription generally starts to run as soon as a debt is due²⁷⁸ and is interrupted by an acknowledgement of liability by the debtor²⁷⁹ or service on the debtor of any process whereby payment is claimed.²⁸⁰ Payment of a debt after it has prescribed (and is thus extinguished) shall be acknowledged as payment of such debt²⁸¹ and a court shall not *mero motu* take note of prescription.²⁸² Although extinctive prescription effects real relief it will only take effect in the most exceptional instances where a debtor has not paid his debt for a substantial period of time; where no process has been served on him; and where he has not acknowledged his indebtedness.

As regards prescription of debts to which the NCA applies,²⁸³ section 31 of the Amendment Act has inserted section 126B which is titled 'Application of prescription on debt' into the NCA. It reads as follows:

- (1) (a) No person may sell a debt under a credit agreement to which this Act applies and that has been extinguished by prescription under the Prescription Act, 1969 (Act No. 68 of 1969).
- (b) No person may continue the collection of, or re-activate a debt under a credit agreement to which this Act applies –
 - (i) which debt has been extinguished by prescription under the Prescription Act, 1969 (Act No. 68 of 1969); and
 - (ii) where the consumer raises the defence of prescription, or would reasonably have raised the defence of prescription had the consumer been aware of such a defence, in response to a demand, whether as part of legal proceedings or otherwise.

The NCA therefore provides additional protection as regards prescribed debts as credit providers are effectively barred from enforcing such debt where the NCA applies thereto.

²⁷⁷ Christie and Bradfield *Christie's* 511.

²⁷⁸ S 12(1).

²⁷⁹ S 14(1).

²⁸⁰ S 15(1).

²⁸¹ S 10(3).

²⁸² S 17(1). This section forms part of ch IV which deals with the general provisions of the Prescription Act.

²⁸³ See ch 4 par 4.3.1 for the application of the NCA.

5.9 Conclusion

In this chapter one proposed and several ancillary debt relief measures for natural person debtors were considered. The proposed pre-liquidation composition²⁸⁴ has the potential to encourage credit providers to rather opt for a negotiated solution in instances where it would probably result in a better return for creditors as compared to the employment of one of the primary and secondary insolvency procedures.²⁸⁵ Although the World Bank *Report* generally regards such undertakings as wasteful²⁸⁶ when measured against international principles and guidelines, the procedure has various positive attributes that may potentially increase its effectiveness.²⁸⁷ These include provisions ensuring that passive creditors are unable to hinder agreements and that formal procedures could be invoked where negotiations fail. Unfortunately the moratorium on debt enforcement does not take effect once an application is lodged, no provision is made for legal aid or debt counselling and costs may pose an obstacle to solving financial problems by making use of the procedure.²⁸⁸

The procedure is intended, in line with international developments in natural person insolvency law,²⁸⁹ to afford those who do not qualify for liquidation proceedings ‘an opportunity for a fresh start which entails a discharge of debts’.²⁹⁰ Unfortunately, the procedure will not reach its goal. There are three basic reasons for this statement. The first is that the (arbitrary) monetary ceiling of R200 000 will exclude a large segment of insolvent debtors from the procedure’s reach. Secondly, only those with income and/or assets will have some form of negotiating power and could therefore potentially benefit from the negotiation stage of the procedure. As was illustrated in chapters 3²⁹¹ and 4, debtors with income and/or assets do presently have some form of statutory recourse in the primary and/or secondary debt relief measures. Thirdly, the very group of debtors (the NINA category) for which the second part of the procedure (that makes provision for a discharge by the master once negotiations have failed) was designed, will not be able to access the procedure. This is because

²⁸⁴ Cl 118 of the 2015 Insolvency Bill.

²⁸⁵ See ch 3 par 3.3 and ch 4.

²⁸⁶ See WB *Report* 46 *et seq* and ch 2 para 2.6.2.1 and 2.7.

²⁸⁷ Ch 2 par 2.7.

²⁸⁸ Par 5.2.

²⁸⁹ Ch 2 par 2.7.

²⁹⁰ 2014 *Explanatory memorandum* 208.

²⁹¹ Par 3.3.

significant costs are involved, namely, that of the administrator and insolvency practitioner as well as travelling expenses (as creditors' domiciles are followed) and no provision is made for free assistance to this group. Furthermore, even if such debtors do find the resources to fund the procedure, it is not suited to their needs as it does not make sense to first channel them through the costly negotiation phase that will generally not be successful. Therefore, the procedure in its current form is more suited to the needs of those natural person insolvents who already have some form of statutory recourse at their disposal. Nevertheless, if the legislature chooses to follow through with the promulgation of the procedure, it is suggested that it be refined by requiring a mere majority in number and value of voting creditors and by rendering the moratorium on debt enforcement effective once the procedure is applied for. It is also suggested that the misleading title of 'pre-liquidation composition' should be substituted with a more neutral title along the lines of 'statutory proposal'.²⁹²

As regards the supervision of the procedure, the proposed exclusion of the courts is in line with international principles and guidelines.²⁹³ As was suggested in chapter 4,²⁹⁴ the NCR could be considered as a supervising body as regards alternative debt relief measures.

Turning to the ancillary measures, it is obvious that none of those discussed constitutes a conventional debt relief measure. However, some of these procedures may be applicable in certain insolvent circumstances and can therefore be applied together with primary and secondary debt relief procedures (as discussed in chapters 3²⁹⁵ and 4) in an effort to assist insolvent debtors.

The two *in duplum* rules were considered in paragraph three and it was established that the statutory rule in terms of section 103(5) of the NCA is not a codification of the common law rule. Furthermore, the statutory rule, when applicable, provides broader protection than the common law rule. One of the reasons for the enhanced

²⁹² Par 5.2.

²⁹³ Ch 2 par 2.7.

²⁹⁴ Par 4.2.8.

²⁹⁵ Par 3.3.

protection is that the statutory rule is not only concerned with outstanding and arrear interest, but with all the amounts specified in section 101(1)(b)–(g) combined. A further significant aspect that results in stronger protection is that once the total charges as provided for in section 101(1)(b)–(g) reach the amount of the unpaid balance, payments made by the consumer, whilst still in default, do not allow the credit provider to charge further costs whilst the consumer is still in (any) default. Another positive aspect from a destitute consumer’s perspective is that the machinery of the statutory rule is not suspended upon the institution of legal proceedings.²⁹⁶

The *in duplum* rules, and specifically the statutory rule (when applicable), are welcome instruments that may be of assistance to some insolvent debtors as they prohibit the accumulation of further costs under certain circumstances. However, these rules will only benefit consumers whose debt has accumulated to an amount that is double the outstanding capital amount or unpaid balance of the principal debt where the statutory rule applies. Nevertheless, in instances where the strict jurisdictional requirements are satisfied, the *in duplum* rules support the broader insolvency system in preventing the further deterioration of insolvent debtors’ financial situations.²⁹⁷

Section 85 of the NCA, dealing with court-ordered debt review, was investigated in paragraph four. It was determined that it provides the consumer, within the context of the NCA and through court involvement, with two alternative routes²⁹⁸ towards a possible re-arrangement of his obligations in terms of section 87 of the NCA. This is so since the court may refer a matter to a debt counsellor with a request that the debt counsellor evaluate the debtor’s circumstances and make a recommendation to court or the court may declare the consumer to be over-indebted and make a debt relief order in terms of section 87. However, before the section may be invoked, a credit agreement must be under consideration in court proceedings (action or application proceedings in the high or magistrate’s court) and there must be an allegation of over-indebtedness. Although section 85 proceedings would generally

²⁹⁶ Par 5.3.

²⁹⁷ *Ibid.*

²⁹⁸ To the s 86 application.

take the form of a request to the court, the court may *suo motu* decide to exercise its discretion in terms thereof provided that the two prerequisites are met. Once a consumer has alleged over-indebtedness in a court or where a credit provider received notice of court proceedings in terms of section 85, the prohibitions on both credit providers and the consumer, as set out in section 88, become relevant.²⁹⁹

As far as the possible purposes for which section 85 was drafted are concerned, it is submitted that it was necessary to provide the courts with a measure to include credit agreements, which are excluded from the debt review procedure (for example when enforcement proceedings have commenced) in circumstances where reason dictates such an inclusion. Through the measure as provided for in section 85 the courts can, as is suggested by Van Heerden, act as an 'abuse-filter' in this regard.³⁰⁰ It is important to note that the court should exercise its discretion judicially and with due regard to the objectives to the NCA. Further, in accepting the wide interpretation that the Supreme Court of Appeal awarded to section 85, the courts' discretion should be exercised by, amongst others, taking cognisance of other relevant provisions of the NCA such as sections 86(1), 86(11), 130(4)(c) and 88(3) and the reasons why a consumer did not opt for these measures where he could have and where such provisions are more suited to his needs. Nevertheless, although only deserving consumers should be assisted by section 85, the observations by Kreuser, namely, that section 85 was drafted for the protection of consumers and that the debt relief measures of the NCA must be used to achieve their objective, are pertinent. Therefore, where possible and reasonable the court must exercise its discretion in favour of deserving consumers.³⁰¹

Even though no reported judgment relating to the second order that a court may make could be found, some of the more apposite decisions pertaining to the first order were considered. Some of these required proof of over-indebtedness. It was also established that certain factors are relevant in assisting the court to exercise its discretion judicially and to ensure that the consumer does not raise over-indebtedness as a delaying tactic with no true intention or a feasible prospect of

²⁹⁹ Par 5.4.

³⁰⁰ Van Heerden 2013 *De Jure* 977.

³⁰¹ Kreuser 2012 *De Jure* 21. See par 5.4.

obtaining relief and eventually satisfying all obligations. Therefore, a consumer should disclose as much as possible relevant information to the court – the most important being a proper argument that an economically feasible restructuring is possible.³⁰²

It was established that section 85 was created as an alternative port to a court sanctioned re-arrangement of a consumer's obligations in terms of his credit agreements. However, save for the fact that section 85 provides an avenue to debt relief from a myriad of procedural locations it is submitted that the actual relief in the end is the same as that provided for in terms of section 87 which was discussed in chapter 4.³⁰³ In this regard and in my opinion the section 85 provisions add two positive elements to the possible relief that the NCA may afford. The first is (limited) increased access in some instances and coupled therewith the possibility of including debts that are generally excluded from the procedure, for instance where debt enforcement proceedings have commenced. The second is that a court may direct a consumer towards relief in instances where the two jurisdictional requirements are met. However, it must be emphasised that where the consumer invokes the section, the possibility of access comes at the price of making out a substantial case as to why the court should exercise its discretion in his favour which poses obvious obstacles to already financially over-committed consumers.³⁰⁴ In conclusion, the fact that the debt review procedure is lacking as a debt relief measure³⁰⁵ became even clearer from discussions relating to section 85. As was noted in the discussion of the debt review procedure, many problems can be eliminated by, amongst others, amending the procedure in accordance with basic international principles and guidelines,³⁰⁶ by for instance excluding secured credit (although special consideration as regards debtors' homes are important) from the procedure's ambit and including agreements where individual enforcement procedures have commenced.³⁰⁷

³⁰² Par 5.4.

³⁰³ See par 4.3.

³⁰⁴ Par 5.4.

³⁰⁵ See ch 4 par 4.3.

³⁰⁶ Par 2.7.

³⁰⁷ See ch 4 par 4.3.

The NCA's reckless credit provisions are regarded as one of its most important features and were discussed in paragraph 5. It was established that the consequences of reckless credit extension can in some instances provide some form of relief to over-committed consumers. It could also be used in conjunction with the primary and secondary debt relief measures.³⁰⁸

The NCA emphasises the encouragement of responsible borrowing by consumers and the discouragement of reckless credit extension by credit providers,³⁰⁹ the latter being done through peremptory assessment requirements and harsh consequences where reckless credit has been extended. Even though the conduct of both consumers and credit providers in relation to the prevention of reckless credit was discussed, the consequences that follow upon a determination that credit was recklessly granted are of special importance to this thesis as the possibility of debt relief lies therein.³¹⁰

Section 83, which sets out the consequences of reckless credit extension, is cast in discretionary terms, but should be read together with section 130(4)(a) which provides that in any proceedings contemplated in the said section and where a court has determined that an agreement was reckless as described in section 80 the court *must* make an order as contemplated in section 83.

Once it is determined that one of the first two types of reckless credit has been extended, a court or the Tribunal may set aside all or part of the consumer's rights and obligations under the agreement or suspend the force and effect of the agreement. The NCA does not set out the effect of the setting aside of an agreement but determines the effect of a suspension in that, whilst the force and effect of an agreement is suspended, the consumer is not required to make any payment under the agreement; no interest, fee or other charge may be charged to the consumer; and the credit provider's rights under the agreement or any law in respect thereof are unenforceable, despite any law to the contrary. After the suspension of the agreement has come to an end all respective rights and obligations of both the credit

³⁰⁸ See ch 3 par 3.3 and ch 4.

³⁰⁹ See preamble and s 3(c).

³¹⁰ Par 5.5.

provider and the consumer in terms of the agreement revive and are fully enforceable except to the extent that a court may order otherwise. As regards the actual relief that a suspension order provides, it will only truly assist mildly over-indebted consumers as it does not provide for a discharge of debt. The only added benefit over a re-arrangement order in terms of section 87³¹¹ is that the relevant credit provider may not charge interest, fees or other charges to the consumer during the period in which the suspension subsists.³¹²

Save for detailing the effect of a suspension to some extent, the NCA is unfortunately silent on a number of issues in relation to section 83(2). These are that it does not set out the effects of the setting aside of an agreement, as previously mentioned, or provide guidelines on how a court should decide between the two aforementioned orders. The NCA further does not differentiate between situations where performance has not occurred and where parties have already performed. It also does not indicate what the rights and obligations of a credit provider would be where the consumer's rights and obligations are set aside partially or completely or on what basis it will be 'just and reasonable in the circumstances' to do so. Even though the courts and commentators have grappled with these questions and have come up with possible solutions, these matters have not been laid to rest. However, what is clear is that the setting aside of an agreement effectively brings an end to the consumer's future obligations, an attribute which has the potential to significantly benefit insolvent debtors.³¹³

Where the third type of reckless credit extension is present the situation differs from the first and second type in that a court or the Tribunal must further consider whether the consumer is over-indebted at the time of the proceedings and only assist the debtor and 'discipline' the creditor if it is found to be the case. Thus, in this regard, the consumer's over-indebtedness not only at the time the agreement was entered into but also at the time the determination is made, is relevant. If the consumer is found still to be over-indebted at the time of the determination, the relevant orders are the suspension of the reckless agreement and the restructuring of other

³¹¹ See ch 4 para 4.3.2 and 4.3.5.

³¹² Par 5.5.

³¹³ *Ibid.*

agreements in accordance with section 87. However, where the consumer is no longer over-indebted, the provision does not provide any recourse for the consumer and does not ‘punish’ the credit provider for his recklessness. Restructuring was discussed in the context of sections 85³¹⁴ and 86³¹⁵ and it was shown that it results in limited relief as once again, no discharge is provided for.³¹⁶

Where *only* the third type of reckless credit is present, an order setting aside the consumer’s obligations is not competent. Nevertheless, it is submitted that more than one type of reckless credit extension may exist in a particular set of facts and that the setting aside of the consumer’s rights and obligations may in some instances also be relevant where a consumer is found to be over-indebted.³¹⁷

In some instances the NCA’s reckless credit provisions offer support for the insolvency system, but are limited in doing so. A suspension order adds to the relief that the NCA offers in that, during the time that a suspension order is effective, the relevant credit provider may not charge the consumer interest, fees and other charges. In terms of a setting aside order, indebtedness is actually curtailed as such an order effectively brings an end to the consumer’s future obligations. However, this order is only competent where the first two types of reckless credit have been established. It is unclear why this more drastic consequence is not commonly available in instances where a consumer has become over-indebted due to the very act of a credit provider, as the result of such conduct is in my opinion more serious than the possible results of the first two types of reckless credit – in instances where it does not also result in over-indebtedness and where the third type of reckless credit extension is thus not relevant.

Paragraph six dealt with a consumer’s extraordinary statutory right to unilaterally terminate an instalment agreement, secured loan or a lease by voluntarily

³¹⁴ See par 5.4.

³¹⁵ See ch 4 par 4.3.

³¹⁶ Par 5.5.

³¹⁷ *Ibid.*

surrendering goods forming the subject of such agreements.³¹⁸ The cooling-off³¹⁹ and early settlement rights³²⁰ were also considered.

The right to voluntary surrender is available to consumers irrespective of whether they are in default or not. Section 127 of the NCA prescribes a specific procedure to be followed pursuant to a voluntary surrender of goods forming the subject of an instalment agreement, secured loan or a lease. These agreements all concern movable property only. A voluntary surrender will be possible in relation to the three types of agreements in two instances, namely, where movable goods are financed under such agreements, irrespective of whether ownership passed or has been retained, and where movable goods are the object of security for amounts due under such agreements.³²¹

A consumer who has voluntarily surrendered property may, in terms of section 127(3), withdraw the notice of termination and resume possession of goods surrendered, provided that the consumer has received a valuation notice and is not in default at the time of withdrawal. The consumer may exercise this right within ten business days pursuant to the valuation notice. It was established that the words 'unless the consumer *is* in default' in section 127(3) do not mean that the consumer was *never* in default. Section 127(3) could well be interpreted that if such consumer was in default, the default was remedied in that the consumer brought payments up to date and has thereby cancelled the default.³²²

It is submitted that the section 127 procedure significantly improves consumers' rights. This is not only as a voluntary surrender of goods is provided for but also as credit providers are obliged to sell the goods as soon as practical for the best price reasonably obtainable. Section 128 further provides a statutory remedy to a consumer who is dissatisfied with the sale of goods. Whether a credit provider has complied with the direction that goods must be sold 'as soon as practicable for the best price reasonably obtainable', will depend on, amongst others, the type of goods,

³¹⁸ Par 5.6.1.

³¹⁹ Par 5.6.2.

³²⁰ Par 5.6.3.

³²¹ Par 5.6.1.

³²² *Ibid.*

market conditions, the condition of the goods and customs and practice in the specific industry. Even though consumers must still settle a shortfall, credit providers may clearly not sell the goods for just any price. The procedure may prove to be especially beneficial to an over-committed consumer as the credit provider bears the burden to ensure that the optimal amount is extracted from the surrendered goods. It is proposed that consumers make use of the section 127 procedure before employing the primary³²³ or a secondary³²⁴ debt relief procedure as it will show good faith and probably improve the consumer's financial situation that will in all likelihood result in a better return for credit providers.³²⁵

As regards the cooling-off right, it was determined that although it leads to the termination of an agreement and could therefore relieve a consumer from future indebtedness, it is not regularly available due to its strict jurisdictional requirements.³²⁶ However, the early settlement rights could, in appropriate circumstances, be used more readily in insolvent circumstances to rid consumers of future debt. Although insolvent debtors do not have surplus income available to settle debt, they can make use of consolidation agreements in this regard.³²⁷

It was recognised that the common law composition, as discussed in paragraph seven, offers an insolvent debtor many benefits as parties are free to negotiate the terms thereof without any restrictions save for those stipulated by the law of contract. Furthermore, debtors may in such instances retain their assets. In this regard three specific constructions of the common law composition were referred to. These are all instances in which parties terminate a contract through the conclusion of a new contract of release, compromise or novation. The common law composition, incorporating the three mentioned constructions thereof, also has less adverse effects on the debtor than the primary³²⁸ and secondary³²⁹ measures and is therefore preferred. However, such compositions are rare due to the necessity of obtaining

³²³ See ch 3 par 3.3.

³²⁴ See ch 4.

³²⁵ Par 5.5.

³²⁶ Par 5.6.2.

³²⁷ Par 5.6.3.

³²⁸ See ch 3 par 3.3.

³²⁹ Ch 4.

consent from all relevant creditors in order to be effective and are therefore not practical in instances where consumers are heavily over-indebted. Debtors' actions in this regard can also in some instances constitute acts of insolvency. In summary, although the common law composition may afford debt relief, the chances of all credit providers reaching a common agreement to such effect are slim. It is consequently submitted that the support that this instrument affords the primary and secondary debt relief procedures is negligible. However, Boraine *et al* propose that compositions may be used to supplement the debt review procedure in instances where some debts are excluded therefrom.³³⁰

The last measure discussed in this chapter is extinctive prescription of contractual debts through the lapse of time. Extinctive prescription has real debt relief as a consequence, although its aim is rather to encourage certainty and fairness. The measure will only in exceptional instances assist debtors, namely, where a debtor has not paid his debt for a substantial period of time; where no process has been served on him; and where he has not acknowledged his indebtedness. The NCA adds to the protection afforded by the Prescription Act in that prescribed debts to which the NCA applies are no longer enforceable.³³¹ Due to its limited applicability this instrument does not generally provide support to the primary³³² and secondary³³³ debt relief procedures.³³⁴

³³⁰ See Boraine *et al* 2012 *De Jure* 267 and par 4.3.4; see also par 3.7.

³³¹ S 126B.

³³² See ch 3 par 3.3.

³³³ Par 4.

³³⁴ Par 3.8.

CHAPTER 6: NEW ZEALAND DEBT RELIEF

SUMMARY

- 6.1 Introduction**
 - 6.2 Historical overview and background**
 - 6.3 Bankruptcy**
 - 6.4 Statutory composition**
 - 6.5 Alternatives to bankruptcy: Statutory procedures**
 - 6.6 Informal arrangements**
 - 6.7 Conclusion**
-

6.1 Introduction

New Zealand has fairly recently reformed its insolvency law by, amongst others, introducing a new Insolvency Act.¹ This Act provides for bankruptcy² and alternative measures,³ in the form of proposals,⁴ summary instalment orders,⁵ and the no asset procedure.⁶ The New Zealand system offers an uncomplicated structure with a simplicity that is especially attractive from a developing country's perspective. Also, in contrast with the South African position, it does not discriminate on financial grounds.⁷ Another reason for investigating the system and comparing its procedures to the South African debt relief measures is the fact that the newly-introduced no asset procedure makes specific provision for the so-called No Income No Asset

¹ Insolvency Act 2006 (hereafter 'the Insolvency Act' or 'the Act'). The Act was assented to on 7 November 2006 and became effective on 3 December 2007 through the Insolvency Act Commencement Order 2007. The Act specifically excludes corporations, associations or a company incorporated or registered under any Act from bankruptcy adjudication or any of the alternative measures. Corporate insolvency is regulated by the Companies Act 1993. This generally reflects the current position in South Africa although the proposed Insolvency Act contemplates a combination of personal and corporate insolvency; see ch 1 par 1.1.

² See pt 2 in general.

³ S 8.

⁴ Pt 5 sub-pt 2, ss 325–339.

⁵ Pt 5 sub-pt 3, ss 340–360.

⁶ Pt 5 sub-pt 4, ss 361–377B.

⁷ See ch 1 par 1.1, ch 3 par 3.5 and ch 4 par 4.4 as regards the South African position in this respect.

(NINA) debtors, a group which, it is submitted, represents the majority of over-indebted or insolvent South Africans at present.⁸

It seems that, unlike the South African debt relief landscape, the New Zealand system generally accepts that its insolvency regime should provide a debt relief measure to all honest but unfortunate individuals who are unable to pay their debts.⁹ In this regard and as far as access is concerned, the system does not discriminate against less fortunate debtors. On the contrary, the New Zealand system specifically provides for their unique needs. The system also does not discriminate in relation to the discharge as, once the debtor is accepted to the system, the bankruptcy, summary instalment orders and no asset procedures provide for the statutory discharge of honest but unfortunate debtors' debt.¹⁰

It follows from the above that the New Zealand system is particularly suited for comparative investigation in relation to South Africa. This chapter thus takes the form of an analysis of the broader New Zealand system by considering all its debt relief procedures both individually and collectively. The analysis includes an evaluation of the system against international principles and guidelines¹¹ and a comparison with the South African situation.¹² In conclusion, inferences are drawn on whether any of the system's elements could be considered for law reform in South Africa.

Paragraph two provides a historic overview of and background to the New Zealand insolvency system for natural persons and is intended to offer a basic understanding of the progression of the system from where it originated to its present state. Paragraph three deals with the bankruptcy procedure. A statutory composition is competent once the first meeting of creditors in bankruptcy procedures has taken place. This measure is considered in paragraph four. Paragraph five is concerned with the statutory alternative procedures to bankruptcy namely, proposals, summary

⁸ See ch 1 par 1.1. See also Coetzee and Roestoff 2013 *Int Insolv Rev* 189.

⁹ See in general chs 3 and 4 and specifically the conclusions to the chapters (para 3.6 and 4.5) as regards the South African position.

¹⁰ See the unfair and unreasonable discrimination resulting from the South African system in ch 1 par 1.1, ch 3 par 3.5 and ch 4 par 4.4.

¹¹ See ch 2 in general and specifically par 2.7.

¹² See ch 3 and ch 4.

instalment orders and the no asset procedure. All statutory procedures are regulated by the Insolvency Act. The research pays special attention to the no asset procedure whose nature is principally foreign to the South African debt relief landscape. For completeness sake, informal arrangements are briefly referred to in paragraph six and the chapter is brought to a close in paragraph seven. The conclusion emphasises the New Zealand imperatives that might be used as yardsticks when considering suggestions for South African law reform.

6.2 Historical overview and background

New Zealand's bankruptcy law as a whole is regulated by legislation, with Guest noting the first indigenous bankruptcy legislation as the Bankruptcy Act 1867. This Act was followed by the Debtors and Creditors Act 1875 and then by the Debtors and Creditors Act 1876. The last Act was substituted by the Bankruptcy Act 1883 and thereafter the Bankruptcy Act 1892.¹³ The latter Act was mostly founded on the prevailing legislation in the United Kingdom. A consolidating Act, the Bankruptcy Act 1908, also modelled on nineteenth century English legislation, more specifically the English Act of 1883,¹⁴ followed as did subsequent amendments in 1927 and 1956.¹⁵ The predecessor to the present 2006 Act, the Insolvency Act 1967,¹⁶ followed. It placed greater emphasis on the economic rehabilitation of the bankrupt¹⁷ and, in line with this ideal, introduced the automatic discharge.¹⁸ Further novel introductions were the proposal and summary instalment order procedures.¹⁹

Even though the 1967 Act was the result of a comprehensive review of bankruptcy law,²⁰ it was not based on a fundamental review of New Zealand insolvency law as it was largely based on English and Australian law reform reports.²¹ Heath mentioned

¹³ Guest 'Introduction: Personal insolvency' 13 and Keeper 2014 *QUT Law Review* 81.

¹⁴ Heath 1999 *Osg Hall LJ* 428 and McKenzie 1968 *NZULR* 210.

¹⁵ Guest 'Introduction: Personal insolvency' 13.

¹⁶ The Act became effective on 1 January 1971. For a discussion of the 1967 Act and specifically the important changes that it brought about see McKenzie 1968 *NZULR* 210. See also Sawyer 1999 *Flinders JL Reform* 183 where he, with reference to the 1967 Insolvency Act, calls for urgent reform of insolvency law and policy in New Zealand.

¹⁷ Guest 'Introduction: Personal insolvency' 13.

¹⁸ See Flintton 1968 *NZLJ* 394–396 in relation to rehabilitation under the 1967 Act.

¹⁹ McKenzie 1968 *NZULR* 210.

²⁰ *Ibid.*

²¹ McKenzie also notes that the committee that undertook the preparatory work for the Bill was able to further draw from Canadian and South African legislation; *idem* 217.

that the aim was to liberalise New Zealand bankruptcy concepts.²² In his 1999 call for legislative reform, he drew attention to the fact that many behavioural changes had occurred in New Zealand due to the deregulation of the New Zealand financial sector (which commenced in 1984)²³ and stated that the Insolvency Act 1967 ‘was, quite simply, never drafted for use in contemporary New Zealand society’.²⁴ Still within the realm of the 1967 Act, he mentioned that the focus of bankruptcy administration²⁵

moved from being quasi-penal in nature towards the dual purpose of (1) maximising returns to creditors, and (2) rehabilitating the debtor. However, there was little of substance to support the second objective, other than a change in the law that made it easier to obtain a discharge from bankruptcy.

The then Ministry of Economic Development,²⁶ being mindful of the need for reform, released the Insolvency Law Reform Bill 2004 and discussion document in April 2004 which was the result of a review of both personal and corporate insolvency law. Guest notes seven planned modifications, namely, modernisation; the improvement of processes; simplicity and efficiency; proceeds distribution that is mostly consistent with pre-bankruptcy rights;²⁷ the maximising of creditor returns; the rehabilitation of bankrupt debtors;²⁸ and the advancement of international co-operation in cross-border insolvencies. The reform seems to differentiate between good faith debtors who are over-indebted to such a degree that public interest calls for a method through which they should be able to obtain a fresh start and irresponsible debtors who should be affected more severely. The then minister of commerce stated that the new no asset procedure mirrored a concern that some of the punitive restrictions of bankruptcy are not suited to individuals with few or no assets and who may have

²² Heath 1999 *Osg Hall LJ* 434.

²³ See *idem* 432–433 in relation to the deregulation of the New Zealand financial sector in general.

²⁴ *Idem* 429. See also Keeper 2014 *QUT Law Review* 84 as regards deregulation and personal insolvency law.

²⁵ Heath 1999 *Osg Hall LJ* 435.

²⁶ This department was incorporated into the Ministry of Business, Innovation and Employment.

²⁷ In South Africa, proceeds distribution is mostly consistent with pre-bankruptcy rights, although the debt review process deviates therefrom in that secured creditors do not receive preferential treatment under the procedure; see ch 3 and 4 in general and ch 4 par 4.3 in particular.

²⁸ In contrast with South African law where the Insolvency Act 24 of 1936 places emphasis on the advantage for creditors requirement and secondary procedures do not provide for a discharge of debt; ch 3 par 3.3.2.2 and ch 4 para 4.2 and 4.3.

become insolvent through no wrongdoing of their own. The emphasis of the proposed procedure was on the fresh start.²⁹

The 2006 Act became operative on 3 December 2007, as was previously stated, and maintains the structure and philosophy of its predecessors. It continues the general alignment with the United Kingdom and Australia. Guest notes that the 2006 Act should be interpreted as a code by which the interests of creditors are both balanced amongst themselves and as a group against the interests of the bankrupt. Even though the 2006 Act does not contain a specific reference to its purposes it seems that the Act's emphasis is on the humane and supportive treatment of bankrupts.³⁰

As far as the history of the administration of the procedures concerning natural persons is concerned, the registries of the then supreme court³¹ and the registrars of each registry were initially appointed as official assignees. The work was later parted out to the official assignee's offices at the time when the commercial affairs division of the Department of Justice was formed. The work was conducted under the Department of Justice but within the said division which administered the courts. Later, the Department of Justice was restructured to, amongst others, exclude the official assignee's work which became part of the Ministry of Economic Development, now the Ministry of Business, Innovation and Employment, which is separate from the administration of the courts.³² The work of the official assignee became known as the New Zealand Insolvency and Trustee Service. It is significant that only official assignees may at present act in the administration of bankrupt estates, but that their resources have been reduced to such an extent that some of the work, for instance services rendered by investigating accountants and investigating solicitors, is now being outsourced to external professionals.³³

²⁹ Guest 'Introduction: Personal insolvency' 14–15. See also Keeper 2014 *QUT Law Review* 80–82 where she illustrates how the procedures contained in the 1967 Insolvency Act were not suited to deal with debtors with few or no assets.

³⁰ Guest 'Introduction: Personal insolvency' 17. *Contra* the South African position which is mostly creditor orientated; ch 3 and ch 4 in general.

³¹ Which is now the high court.

³² The administration of courts still falls under the Ministry of Justice. In South Africa the Department of Justice and Constitutional Development is mostly responsible for insolvency-related matters except for the debt review procedure that resorts under the Department of Trade and Industry; see ch 1 par 1.1.

³³ Guest 'Introduction: Personal insolvency' 13–14.

Bankruptcy is now mostly an administrative procedure.³⁴ In this regard the assignee generally administers property, considers creditors' claims³⁵ and distributes the proceeds of the estate.³⁶ In addition to his administrative function, the assignee also has a duty to investigate and commence criminal proceedings in relation to insolvency legislation.³⁷ Thirdly, he is the guardian of the public interest.³⁸ Also, the office of the assignee nowadays provides for a state-funded 'one stop shop' for insolvent debtors which will become clearer from the discussion of the alternative procedures to bankruptcy below.³⁹ It is apparent that the assignee assumes responsibility for various matters that previously fell within the jurisdiction of the courts.⁴⁰ However, Telfer notes that there might potentially be conflicts of interest as the '[a]ssignee will play the role of fact finder, adjudicator and creditor representative, as well as a counsellor to the debtor'.⁴¹

6.3 Bankruptcy

6.3.1 General

Bankruptcy⁴² and the process regulating it are provided for in part 2 of both the Act⁴³ and the regulations.⁴⁴ Bankruptcy is only available to individuals⁴⁵ and may be applied for by a creditor (or creditors)⁴⁶ of the debtor or the debtor himself.⁴⁷ According to section 10, adjudication occurs when a debtor is adjudicated bankrupt. This is when a creditor applies to the high court for an adjudication order and such

³⁴ See in contrast ch 3 in that the South African sequestration procedure is heavily reliant on the courts.

³⁵ See reg 12 in relation to the creditor's claim form.

³⁶ See in general s 217 read with sch 1. In terms of s 224 the assignee may use his discretion in the administration of the bankrupt's property. However, he must have due regard to creditors' resolutions. In South Africa the trustee takes care of these functions under the supervision of the master of the high court; see ch 3 in general.

³⁷ S 438(1).

³⁸ See Morris 'Powers and duties of official assignee' 174 and authority cited there.

³⁹ See par 6.5.

⁴⁰ See Telfer 'New Zealand bankruptcy law reform: The new role of the official assignee and the prospects for a no-asset regime' 248.

⁴¹ *Ibid.* See also 256–60.

⁴² Compare sequestration in the South African system; ch 3 par 3.3.

⁴³ Pt 2 of the Act consists of ss 7–100.

⁴⁴ Insolvency (Personal Insolvency) Regulations 2007. Reg 2 provides that the regulations came into effect on 3 December 2007. Pt 2 consists of regs 6–19.

⁴⁵ See s 6(a).

⁴⁶ However, international principles and guidelines caution that creditor petitions may be misused; ch 2 par 2.7.

⁴⁷ The South African system also provides for applications by both creditors and the debtor; ch 3 par 3.3.2.1.

order is made⁴⁸ or when the debtor applies to the assignee for adjudication.⁴⁹ The courts are generally not involved in instances where debtors apply for their own adjudication.⁵⁰ Bankruptcy adjudication affects the debtor in his personal capacity.⁵¹

6.3.2 Access requirements and effect thereof

A creditor may apply for a debtor's adjudication as bankrupt, with section 13 setting out four substantial requirements which should be complied with in order to proceed with the application.⁵² The only procedural requirement seems to be the application to the high court (for bankruptcy adjudication) itself. Section 13 provides that a creditor may bring such an application if the debtor owes the creditor NZ\$1 000 or more or where more than one creditor applies jointly, that the debtor owes a total of NZ\$1 000 or more to those creditors between them.⁵³ It is to be noted that according to section 14 a secured creditor⁵⁴ may only bring such an application where the amount of the debt exceeds the value of the charge⁵⁵ by at least NZ\$1 000. Other requirements are that the debtor has committed an act of bankruptcy within the

⁴⁸ Ss 10(2)(a) and 36. Ss 13–44 regulate adjudication by court on application by a creditor. S 56(1) provides that the date of adjudication in such instances is the date and time when the order of adjudication is made. The South African counterpart of the process is termed compulsory sequestration proceedings; ch 3 par 3.3.2.1.

⁴⁹ S 10(2)(b). Ss 45–49 regulate adjudication on a debtor's application. S 56(2) provides that the date of adjudication in such instances is the date and time the application is filed by the debtor. According to s 49(2) an application is filed when endorsed by the assignee as having been received. In South Africa, all sequestration applications are made to the high court. The South African debtor's application is known as the voluntary surrender of an estate; ch 3 par 3.3.2.1.

⁵⁰ The fact that courts are not involved is in accordance with international principles and guidelines; ch 2 par 2.7.

⁵¹ See Guest 'Process for procuring bankruptcy' 31.

⁵² Compare South African compulsory sequestration application requirements; ch 3 par 3.3.2.1.

⁵³ S 13(a).

⁵⁴ S 3 defines a secured creditor as 'a person entitled to a charge on or over property owned by a debtor'.

⁵⁵ Section 3 defines a charge as including
a right or interest in relation to property owned by a debtor, by virtue of which a creditor of the debtor is entitled to claim payment in priority to other creditors; but does not include a charge under a charging order issued by a court in favour of a judgment creditor.

preceding three months⁵⁶ and that the debt is in a certain amount.⁵⁷ The debt must further be payable immediately or at a certain date in future.⁵⁸ An application for adjudication may only be withdrawn by a creditor with the court's permission.⁵⁹

The most commonly used act of bankruptcy is the first listed in the Act, namely, 'Failure to comply with bankruptcy notice'.⁶⁰ A bankruptcy notice is a notice issued by the registrar of the high court on request of a creditor after a final judgment or order for any amount has been obtained and where execution has not been stayed by a court. This act of bankruptcy is committed when the debtor fails to comply with the notice within ten working days after service thereof and where he cannot satisfy the court that he has a cross claim against the creditor.⁶¹ Relying on this particular act of bankruptcy is according to Guest the most practical route for creditors to follow as it formalises a 'last chance' to pay and (upon non-payment) is easy to prove.⁶²

Sections 31 to 35 set out the effect of a creditor's application on execution procedures. These are that the application creditor may not, save with the court's permission, commence or continue execution procedures against the debtor (in relation to property or person) to recover debt on which the application is based.⁶³ As far as execution procedures in relation to other creditors are concerned, the debtor or any creditor may, upon the filing of the application for adjudication, apply to court

⁵⁶ S 13(b) and s 16(1). The acts of bankruptcy are set out in ss 17–28, some of which are similar to their South African counterparts as set out in s 8 of the Insolvency Act. However, in South African law the creditor bringing the application for compulsory sequestration has the option of either proving insolvency or that an act of insolvency has been committed; see ch 3 par 3.3.2.1. Although New Zealand law does not provide for the adjudication of a debtor on the separate ground of insolvency, some of the acts of bankruptcy indirectly provide therefor; see s 23 titled 'Admission to creditors of insolvency'. Before a creditor may proceed on this ground not only must the debtor have admitted insolvency but the majority in number and value of creditors present at the meeting must have required the debtor to file an application for adjudication. In instances where the debtor has agreed to file such an application, he must not have done so within two working days after the meeting. Nevertheless, relying on acts of bankruptcy is, according to international principles of sound insolvency systems for natural persons, out-dated as the focus should rather be on inability to pay than on 'wrongful' acts of the debtor; ch 2 par 2.7.

⁵⁷ S 13(c).

⁵⁸ S 13(d).

⁵⁹ S 15.

⁶⁰ S 17.

⁶¹ See s 17(1); 17(3) and 17(4) read together with Guest 'Process for procuring bankruptcy' 33–35.

⁶² Guest 'Process for procuring bankruptcy' 33. See s 29 for the form of the bankruptcy notice. The notice explains to the debtor that it is a last change in that he is provided with options, failing which the consequences set out in the notice will follow.

⁶³ S 31.

to suspend the issue or continuance of such procedures. The court may suspend or allow the procedures to continue on terms and conditions (if any) that it may deem fit.⁶⁴ An automatic stay of execution proceedings becomes effective on adjudication.⁶⁵

After a creditor's application for adjudication has been filed but before an order of adjudication has been made, the court may appoint the assignee as receiver and manager of all or part of the debtor's property and authorise him to take certain steps such as to take possession of property and to sell items that are likely to deteriorate in value rapidly.⁶⁶ The invocation of this procedure will, as can also be detected from the steps that the court may authorise the assignee to take, be necessary in instances where urgent interim steps are needed to secure the position of a debtor whose circumstances are hastily deteriorating to the prejudice of creditors.⁶⁷ Such an application is brought by a creditor and has the effect that execution processes are automatically stayed. However, a creditor or other interested person may apply to court for an order to continue such processes and the court may make an order on terms and conditions that it may deem fit.⁶⁸ The appointment of the assignee as receiver and manager must be confined to what is necessary for conserving property.⁶⁹

The court has a number of options when considering the creditor's application for adjudication. It may firstly adjudicate the debtor bankrupt after the requirements in terms of section 13 have been met⁷⁰ and it may also 'halt'⁷¹ the application on terms

⁶⁴ S 32.

⁶⁵ S 76. In South Africa, enforcement proceedings are similarly automatically stayed once a sequestration order is granted; see ch 3 par 3.3.1. International guidelines favour the position where the moratorium on debt enforcement commences once a bankruptcy petition is filed; ch 2 par 2.7.

⁶⁶ S 50(1), (2); and (3) and s 51.

⁶⁷ Guest 'Process for procuring bankruptcy' 54. See also s 50(4).

⁶⁸ S 50(1) and s 53. See s 54 regarding the effect of stayed execution processes.

⁶⁹ S 50(4).

⁷⁰ S 36. After adjudication, the bankrupt must file a statement of affairs at the assignee; s 67. See reg 6 in relation to the debtor's statement of affairs which, amongst others, prescribes the information that the statement must contain.

⁷¹ See Guest 'Process for procuring bankruptcy' 60–62 for a discussion of instances in which a 'halt' has been ordered. This may for instance be where a debtor has instituted action against a party and there are prospects of recovering sufficient proceeds to cover all his debts to his creditors. Another example is where a summary instalment order is in place and the majority of creditors are satisfied with the order and the manner in which the debtor gives effect thereto.

Footnote continues on next page

and conditions and for a period that it may deem fit.⁷² It may further refuse the application if,⁷³ in its discretion,⁷⁴

- (a) the applicant creditor has not established the requirements as set out in section 13; or
- (b) the debtor is able to pay his or her debts; or
- (c) it is just and equitable that the court does not make an order of adjudication; or
- (d) for any other reason an order of adjudication should not be made.

Guest refers to instances where the courts refused adjudication and specifically mentions *In re Betts; Ex parte Betts*⁷⁵ where the lack of assets constituted such reason.⁷⁶ This begs the question whether this sentiment indirectly introduces the advantage for creditors requirement in New Zealand bankruptcy law.⁷⁷ However, this comment should be read within the context of creditors' petitions specifically. In this regard, the case of *Baker v Westpac Banking Corporation*⁷⁸ is also relevant. Here the Court of Appeal held that the interests of all parties and that of the public should be considered by the court.⁷⁹ The court cautioned that a creditor does not have an automatic title to an adjudication order upon proving the necessary grounds.⁸⁰ It stated that thought needs to be given to possible oppressive use of the procedure,⁸¹

These instances are over and above the provisions of ss 42 and 43 setting out specific occasions in which a halt may be appropriate, namely, 'Halt or refusal of application when judgment under appeal' and 'Court may halt application while underlying debt determined'.

⁷² S 38.

⁷³ S 37.

⁷⁴ See ch 3 par 3.3.2.1 in relation to South African courts' discretion.

⁷⁵ [1897] 1 QB 50.

⁷⁶ Guest 'Process for procuring bankruptcy' 59.

⁷⁷ It was stated in the case that a court is not at the application stage of the proceedings in a position to know whether statements by a debtor that he does not have assets which could be dealt with in bankruptcy and no prospect of ever having any are true and cannot accept such as sufficient grounds for not awarding a receiving order. However, all three presiding judges agreed that *in casu* the court was convinced, not only by statements of the debtor but from the circumstances of the case, that there were no assets or a prospect of any coming into existence and that a receiving order would be a waste of money and costs. The court thus exercised its discretion by refusing the order; *In re Betts, ex parte Betts* 52–54. In the South African system, benefit to creditors must be proved in order to obtain a sequestration order (ch 3 par 3.3 in general) while in the New Zealand system it must be proved that there are or will definitely be no assets which could be dealt with in bankruptcy in order for the order not to be awarded.

⁷⁸ CA212/92, 13 July 1993.

⁷⁹ *Baker v Westpac Banking Corp* 4–5. The South African system is solely concerned with the interests of creditors which form the basis thereof. The interests of debtors and the public are for the most part ignored; ch 3 par 3.3 in general.

⁸⁰ *Baker v Westpac Banking Corp* 5.

⁸¹ This is in line with international principles and guidelines that caution against creditor misuse; ch 2 par 2.7.

the absence of assets, the public interest of administering the debtor's affairs for a period and the disqualifications accompanying bankruptcy.⁸²

Sections 12, 45, 46 and 49 are relevant to the debtor's application. In terms of section 12(1) a debtor may be adjudicated bankrupt by filing an application with the assignee. The debtor's application prescribes both substantive and procedural requirements.⁸³ The substantive requirement is set out in section 45 which provides that a debtor may file an application if the debtor has combined debts of at least NZ\$ 1 000.⁸⁴ Sections 46 and 49 are concerned with procedural requirements. Section 46 provides that a debtor may not file an application for adjudication before filing a statement of affairs⁸⁵ which may be rejected by the assignee if it is incorrect or incomplete. In terms of section 49(1), in order to file an application for adjudication, the debtor must complete the prescribed form,⁸⁶ which must be lodged with the assignee in accordance with the prescribed procedure. As was mentioned, section 49(2) provides that the application is filed when endorsed by the assignee as having been received. Consequently and according to section 47 a debtor who files such an application is automatically adjudicated bankrupt the moment the application is filed.⁸⁷ The filing has the same consequences as if the debtor had been adjudicated bankrupt by the court.⁸⁸

6.3.3 General process once an application has been accepted

Once an application for bankruptcy has been accepted, either through an application to court in forced proceedings or through the assignee in voluntary proceedings, the

⁸² *Baker v Westpac Banking Corp* 5. See also Guest 'Process for procuring bankruptcy' 60. From this judgment it seems that the New Zealand courts are following the international best practice of considering the interests of not only the creditor(s), but also that of the debtor and society; ch 2 par 2.7.

⁸³ S 12(2) and (3). This is also the situation in South African law; ch 3 par 3.3.2.1.

⁸⁴ It is interesting that insolvency need not be proven. Furthermore, the advantage for creditors requirement is not set as a prerequisite and the debtor also need not prove that there will be sufficient free residue to cover the costs of bankruptcy. In South African law these are fundamental requirements and major obstacles as far as access to debt relief is concerned; ch 3 par 3.3.2. It seems that the New Zealand system adheres to the international principle that access should be as wide as possible; ch 2 par 2.7.

⁸⁵ See regs 6 and 8.

⁸⁶ See further reg 7. Reg 7(3) provides that the fee payable for making the application is NZ\$ 200.

⁸⁷ S 47(1).

⁸⁸ S 47(2). Thus, the moratorium on individual debt enforcement, in accordance with s 76, becomes effective once the application is filed. This is in line with international principles and guidelines; see ch 2 par 2.7.

process essentially takes the same form. All provable debt is included⁸⁹ in the procedure and is generally automatically discharged after a period of three years.⁹⁰ Provable debts are those which the bankrupt owes at the time of adjudication or thereafter but before discharge.⁹¹ However, secured debt receives special treatment. Secured creditors⁹² have a number of options at their disposal.⁹³ They may realise the property,⁹⁴ value the property and prove in bankruptcy as an unsecured creditor for the balance,⁹⁵ or surrender the property to the assignee and prove in bankruptcy as an unsecured creditor for the whole of the outstanding amount.⁹⁶

On adjudication, all property⁹⁷ belonging to the bankrupt generally vests in the assignee.⁹⁸ Property acquired after adjudication but before discharge also vests in the assignee.⁹⁹ This includes income of the bankrupt. However, income will rarely be collected by the assignee due to its usually modest nature and the common law principle that a bankrupt is entitled to retain from earnings that which is necessary to

⁸⁹ Ss 231 and 232. According to s 231(1) provable debt is a debt or liability that a creditor may prove in bankruptcy.

⁹⁰ The most recent international report supports a period of no longer than three years; *WB Report* 86. See also ch 2 par 2.7. S 304(2) lists debts that are provable, but from which the bankrupt is not released on discharge. Examples are debt or liability incurred by fraud, maintenance debt or amounts payable under the Child Support Act 1991. See ch 2 par 2.7 in that international principles and guidelines generally favour a wide discharge with the exclusion of maintenance debts. See pt 4 sub-pt 1 relating to discharge from bankruptcy. In South African law an automatic discharge is generally effected only after a period of ten years; ch 3 par 3.3.4.

⁹¹ S 232(1). S 232(2) sets out debts that are not regarded as provable debts in bankruptcy. These are fines, penalties, sentence of reparation or other order for payment of money made following a conviction or order in terms of s 106 of the Sentencing Act 2002. International principles and guidelines do not recommend exceptions for fines and damages; ch 2 par 2.7.

⁹² A secured creditor is defined in s 3 as 'a person entitled to a charge on or over property owned by a debtor'.

⁹³ S 243. See also Guest 'Property divisible amongst creditors' 124 *et seq.*

⁹⁴ If permitted to do so; s 243(1)(a).

⁹⁵ S 243(1)(b).

⁹⁶ S 243(1)(c). International guidelines accept that secured debt is generally excluded from the discharge; ch 2 par 2.7. In South African law, the trustee sells secured property, but subject to costs in relation to maintenance, conservation and realisation, secured creditors are generally first in line as regards such proceeds; ch 3 par 3.3.1.

⁹⁷ Property is defined in s 3 as

Property of every kind, whether tangible or intangible, real or personal, corporeal or incorporeal, and includes rights, interests, and claims of every kind in relation to property however they arise.

⁹⁸ S 101. Except those exempted in terms of s 158. However, international principles and guidelines provide that the focus on assets is all but a formality as most debtors do not have assets of value. In any event, the liquidation procedure should be linked with property exemptions and in this regard a standards-based approach that exempts most property from the estate as a matter of course is suggested for jurisdictions where debtors have limited personal assets; ch 2 par 2.7.

⁹⁹ S 102.

sustain himself and his family to a reasonable standard.¹⁰⁰ In this regard section 163 is important as the assignee may make an allowance out of the bankrupt's property to the bankrupt or one of his relatives or dependants for his or their support.¹⁰¹

As far as the general vesting of property is concerned not all property vests in the assignee as there are a number of statutory exceptions, such as property held on trust,¹⁰² rights of execution creditors¹⁰³ and property in relation to second bankruptcies.¹⁰⁴ There are also statutory exceptions resulting from other legislation¹⁰⁵ and at common law certain rights of personal action for compensation do not vest in the assignee.¹⁰⁶ Sections 158 and 159 deal with provision for the bankrupt during bankruptcy and provide that the bankrupt may retain certain assets.¹⁰⁷ However, the retention of such assets does not affect rights under a charge or hire purchase agreements.¹⁰⁸ The assets that the bankrupt may retain are

- a. Tools of trade – the maximum value¹⁰⁹ being fixed in the discretion of the assignee;¹¹⁰

¹⁰⁰ See Guest 'Property divisible amongst creditors' 91 and authorities cited there. S 147, amongst others, provides that a bankrupt may be required to contribute to payment of debts if required by the assignee. However, the assignee must have regard to the circumstances of the bankrupt and make reasonable allowance for the maintenance of the bankrupt and his relatives and dependants. This is in accordance with the international principles and guidelines as regards the object of rehabilitation; ch 2 par 2.7.

¹⁰¹ In terms of s 164 the assignee may allow the bankrupt to retain money up to a maximum of NZ\$1 000 for the maintenance of himself and his relatives and dependants that are in his possession or in a bank account at the time of adjudication.

¹⁰² S 104.

¹⁰³ S 108.

¹⁰⁴ S 134.

¹⁰⁵ S 105(2) provides that ss 101–104 do not affect the operation of other legislation that prevents property from vesting in the assignee. Examples are the family home as protected by the Joint Family Homes Act 1964 (see s 4(b) of the Insolvency Act 2006); Maori land as protected by the Maori Land Act 1993; retirement allowances and other money payable under the Government Superannuation Fund in terms of the Government Superannuation Fund Act 1956; and benefits payable under the Social Security Act 1964. See in general Guest 'Property divisible amongst creditors' 110. As regards the protection of the family home by means of the Family Homes Act 1964 see Steyn *Statutory regulation* 446–450.

¹⁰⁶ See Guest 'Property divisible amongst creditors' 97–98 and authorities cited there.

¹⁰⁷ Compare with the South African system in relation to excluded or exempted property; ch 3 par 3.3.3. As was noted above, international guidelines favour the position where most property are exempted from the estate as a matter of course; ch 2 par 2.7.

¹⁰⁸ S 160.

¹⁰⁹ S 158(2) provides that, for purposes of ss 158 and 159, maximum value means the value specified in subsection (3).

¹¹⁰ S 158(3)(a).

- b. necessary household furniture and effects¹¹¹ – the maximum value being fixed in the discretion of the assignee;¹¹²
- c. a motor vehicle – maximum value NZ\$5 000;¹¹³ and
- d. necessary tools of trade and household furniture and effects that are worth more than the maximum value as consented to by creditors by way of an ordinary resolution.¹¹⁴

Bankruptcy places substantial personal restrictions on a bankrupt such as a restriction on entering business without the consent of the assignee¹¹⁵ or the court;¹¹⁶ to travel overseas without the assignee's consent;¹¹⁷ and to obtain credit under certain circumstances.¹¹⁸ The Act also confers certain duties on the bankrupt which can be categorised in terms of the duty to provide information;¹¹⁹ duties in relation to property;¹²⁰ and the duty to carry out certain actions.¹²¹

6.3.4 Discharge and annulment

As was already emphasised, a bankrupt is generally automatically discharged from bankruptcy after a period of three years from filing a statement of affairs under section 46 or section 67 has lapsed.¹²² A bankrupt may also apply to court for his

¹¹¹ These include clothing for the bankrupt and his relatives and dependants.

¹¹² S 158(3)(b).

¹¹³ S 158(3)(c). South African insolvency law is not familiar with such an exclusion; ch 3 par 3.3.3.

¹¹⁴ S 159.

¹¹⁵ See reg 10 in relation to the bankrupt's application for the assignee's consent to enter into business.

¹¹⁶ S 149.

¹¹⁷ Ss 426 and 433(1)(f). See also reg 11 regarding the bankrupt's application to the assignee to travel overseas.

¹¹⁸ S 433A: a bankrupt commits an offence if he alone or jointly obtains credit of NZ\$1 000 or more. He also commits an offence if he incurs liability to a person of NZ\$1 000 or more for the purpose of obtaining credit for another. Compare in general the South African system; ch 3 par 3.3.1.

¹¹⁹ Ss 142–146. These, amongst others, include the duty to provide the assignee with financial information; accounting records; information relating to property; income and expenditure; and notifications in relation to a change in personal information.

¹²⁰ Ss 139–141. These, amongst others, include the duty to disclose property acquired before discharge; the delivery of property on demand; and the duty to take all required steps in relation to property and the distribution of proceeds to creditors.

¹²¹ Guest 'Duties of bankrupt' 122. S 138 sets out the general duty of the bankrupt, namely, to assist in the realisation of property and the distribution of proceeds amongst creditors to the best of his ability. Ss 139–146 contain specific duties, as referred to above, although not all inclusive.

¹²² S 290(1), *contra* the South African position where an automatic discharge only takes place once a period of ten years has lapsed; ch 3 par 3.3.4.

discharge at an earlier stage.¹²³ There are three instances when an automatic discharge will not take place, namely, where the assignee or a creditor has objected to the automatic discharge and the objection has not been withdrawn by the end of the three-year period;¹²⁴ where the bankrupt has to be publically examined under section 173¹²⁵ which examination has not been completed;¹²⁶ or where the bankrupt is not discharged from a previous bankruptcy.¹²⁷ In any of these situations, the assignee must summon the bankrupt to be publicly examined by the court in relation to his discharge whereafter such examination must take place.¹²⁸ In these instances and where the bankrupt has applied for an early discharge in terms of section 294, the assignee must file a report in court.¹²⁹ This report should relate to the bankrupt's affairs; causes of bankruptcy; bankrupt's performance of his statutory duties; manner in which the bankrupt has obeyed court orders; bankrupt's conduct prior to and after adjudication; and any other matter that would be of assistance to the court in deciding on the bankrupt's discharge.¹³⁰ In the event that a creditor intends to oppose the discharge on grounds other than those mentioned in the assignee's report, the creditor must give notice to the assignee and the bankrupt setting out the grounds thereof.¹³¹ As the assignee acts as the guardian of public interest in bankruptcy matters he has the duty to oppose the possibility of a discharge where public interest calls therefor.¹³² The onus of proof obviously follows any person who wishes to change the ordinary course of proceedings. Therefore, where the bankrupt seeks an order for discharge earlier than the three year period, he must persuade the court to grant such an order. Similarly, where the assignee or a creditor objects

¹²³ S 294(1). The hearing of such an application must be conducted in accordance with s 177; s 294(2). However, where a court has previously refused such an application and has specified a date before which the bankrupt may not apply for a discharge, the bankrupt must not apply therefor before such date; s 294(2).

¹²⁴ S 290(2)(a) read with ss 292 and 293.

¹²⁵ S 173 provides for a public examination in court in instances where the assignee or creditors require same before a discharge takes effect.

¹²⁶ S 290(2)(b) read together with s 295.

¹²⁷ S 290(2)(c).

¹²⁸ S 295(1).

¹²⁹ S 296(1).

¹³⁰ S 296(2).

¹³¹ S 297. The notice must not be provided less than five working days before the application is to be heard; reg 19.

¹³² See Crossland 'Discharge from and annulment of bankruptcy' 223 and authorities cited there. The New Zealand system, in accordance with international guidelines, strives to balance the rights of creditors, the debtor and society; ch 2 par 2.7.

to the automatic discharge, he should satisfy the court that it is not desirable to allow the automatic discharge to take place.¹³³

Section 298 deals with the court's powers in relation to the discharge. Section 298(1) provides that a court, when entertaining an application in terms of section 294 or conducting an examination in terms of section 295 may, having regard to all the circumstances,

- (a) immediately discharge the bankrupt; or
- (b) discharge the bankrupt on conditions (which may include a condition that the bankrupt consents to any judgment or order for the payment of any sum of money);¹³⁴ or
- (c) discharge the bankrupt but suspend the order for a period; or
- (d) discharge the bankrupt, with or without conditions, at a specified future date; or
- (e) refuse an order of discharge, in which case the court may specify the earliest date when the bankrupt may apply again for discharge.

The leading judgment in relation to an early discharge of a bankrupt is that of the Court of Appeal in *ASB Bank Ltd v Hogg*.¹³⁵ In *Hogg*, which was decided on section 108 of the 1967 Act which is akin to section 294 of the present Act, it was held that¹³⁶

the legislation recognises that each case will be different, that the relevant factors may vary from case to case and that the exercise of the discretion must be governed by the circumstances of the particular case having regard to the guidance provided by a consideration of the scheme and purpose of the legislation. In providing for automatic discharge after three years, the legislation recognises that it is not in the public interest that the bankruptcy should endure indefinitely. In providing for earlier discharge, s 108 recognises that continuing the bankruptcy to the end of the three years may not be in the public interest. Whether or not it is will be a matter for decision on the particular facts. In that regard, guidance is provided by s 109(2)¹³⁷ which lists matters on which the assignee is to report to the High Court in such a case. The Court is to consider the assignee's report as to the affairs of the bankrupt, the causes of the bankruptcy, the manner in which the bankrupt has performed the duties imposed on him or her under the Act and his or her conduct both before and after the bankruptcy, and also as to any other fact, matter or circumstance that would assist the Court in making its decision. Clearly the Court apprised of the

¹³³ Crossland 'Discharge from and annulment of bankruptcy' 216.

¹³⁴ S 303 provides that where a bankrupt cannot comply with all or any of the conditions he may apply to court for an absolute discharge. The court may so discharge the bankrupt if satisfied that the inability to adhere to the conditions is due to circumstances for which the bankrupt should not reasonably be held responsible.

¹³⁵ [1993] 3 NZLR 156. See Crossland 'Discharge from and annulment of bankruptcy' 224.

¹³⁶ *ASB Bank v Hogg* 157–158.

¹³⁷ This subsection is similar to s 296(2) of the existing Act.

matter will consider the legitimate interests of the bankrupt, the creditors and wider public concerns,¹³⁸ but it is neither required nor entitled to impose threshold requirements in the exercise of the discretion so as to derogate from the breadth of the powers conferred under s 110. The applicant has the onus, in the sense of adducing evidence, to show good cause for ordering an early discharge, but his obligation goes no further than that.

It was held that the bankrupt may be questioned on issues that may lead to the possible disclosure of further assets and matters relevant to the public interest.¹³⁹ However, conduct unrelated to the bankruptcy cannot be taken into consideration during the examination as it was held that¹⁴⁰

[o]nly such conduct or affairs as may or can have had some effect upon the bankruptcy itself ought to be taken into consideration.

A creditor or the assignee may apply to court to reverse an absolute discharge in the two-year period following the discharge or two years after the discharge takes effect in instances where it was conditionally awarded or suspended.¹⁴¹ The court may, at such or a later stage, make a new order relating to the bankrupt's discharge.¹⁴² However, the discharge may only be reversed if the bankrupt has received notice of the application¹⁴³ and the court is satisfied that there are facts which were not known to the court when it ordered the discharge and if they were known, would have justified a refusal of the discharge or led to a conditional discharge.¹⁴⁴ The effect of such a reversal does not prejudice or affect rights or remedies that persons, other than the bankrupt, would have had, had the reversal not taken place.¹⁴⁵ Further, where the bankrupt has acquired vested property after the discharge, such property shall

¹³⁸ As was mentioned above, the New Zealand system strives to balance the interests of debtors, creditors and society which is in line with international elements of progressive insolvency systems for natural persons; ch 2 par 2.7.

¹³⁹ *In re Jawett* [1929] 1 Ch 108 112. See also Crossland 'Discharge from and annulment of bankruptcy' 224.

¹⁴⁰ *In re Baker; Ex parte Constable; In re Jones; Ex parte Jones* (1890) 25 QBD 285 (CA) 293. See also Crossland 'Discharge from and annulment of bankruptcy' 224.

¹⁴¹ S 300(1).

¹⁴² S 300(2).

¹⁴³ S 301(1)(a).

¹⁴⁴ S 301(1)(b). Nevertheless, the court must not reverse the discharge if the facts on which the application is based were known to the applicant or could have been known by making inquiries with reasonable diligence at the time the discharge was awarded; s 301(2).

¹⁴⁵ S 302(1).

vest in the assignee subject to encumbrances and must be applied to pay debts incurred after the discharge had taken effect.¹⁴⁶

As was stated above, the effect of the discharge is that the bankrupt is released from all provable debts subject to certain exceptions.¹⁴⁷ However, the discharge does not release partners and persons other than the bankrupt.¹⁴⁸ Further, the court may restrict the bankrupt from engaging in business after the discharge without the court's permission.¹⁴⁹ The discharged bankrupt remains obliged to assist the assignee in the realisation and distribution of property vested in the assignee.¹⁵⁰

New Zealand law provides for certain grounds on which a court may annul an adjudication on application of the assignee or another interested person.¹⁵¹ Similarly, where the adjudication was made on a debtor's application, the assignee may annul an adjudication on application by an interested person or on own initiative on the same grounds.¹⁵² These grounds are if the court or assignee¹⁵³ considers that there should not have been an adjudication of bankruptcy;¹⁵⁴ or is satisfied that the debts have been paid in full and that the assignee's fees¹⁵⁵ and costs¹⁵⁶ incurred in the

¹⁴⁶ S 302(2).

¹⁴⁷ The following debts are excluded from the discharge:

- (a) any debt or liability incurred by fraud or fraudulent breach of trust to which the bankrupt was a party;
- (b) any debt or liability for which the bankrupt has obtained forbearance through fraud to which the bankrupt was a party;
- (c) any judgment debt or amount payable under any order for which the bankrupt is liable under section 147 or section 298;
- (d) any amount payable under a maintenance order under the Family Proceedings Act 1980;
- (e) any amount payable under the Child Support Act 1991.

Ss 147 and 298 were discussed above.

¹⁴⁸ S 306.

¹⁴⁹ S 299.

¹⁵⁰ S 307.

¹⁵¹ S 309(1). In South Africa, both provisional and final sequestration orders may be rescinded. However, legislation does not set specific grounds therefor; ch 3 par 3.3.1.

¹⁵² S 310(1) read together with s 310(3).

¹⁵³ S 309(1).

¹⁵⁴ In this instance the adjudication is annulled from the date of the adjudication; ss 309(3)(a) and 310(4)(a).

¹⁵⁵ Reg 18(1) provides that the rates of remuneration for the assignee and his staff are as follows:

- (a) the Assignee and Deputy Assignee: \$200 per hour;
- (b) legal and accounting staff: \$200 per hour;
- (c) insolvency officers: \$140 per hour.

¹⁵⁶ According to reg 17, the assignee is not required to incur any expenses in relation to the estate if there are no available assets, but may do so if the assignee has obtained a guarantee from

Footnote continues on next page

bankruptcy have been settled; or considers that the liability of the bankrupt to pay his debts should be revived as a substantial change in financial circumstances since the date of adjudication has emerged; or where the court has approved a composition under subpart 1 of part 5.¹⁵⁷ The effect of an order of annulment is that all property of the bankrupt that is vested in the assignee and not sold or disposed of reverts in the bankrupt without the necessity of further procedural requirements.¹⁵⁸ Further, anything done or made by the assignee before the annulment remains valid and has the effect as if it had been made or done by the bankrupt while no adjudication was effective.¹⁵⁹

6.3.5 Effect of statutory alternative debt relief measures on bankruptcy

As far as the effect of statutory alternative debt relief procedures on the bankruptcy procedure is concerned, the provisions of section 41 should be noted. It provides that where a debtor has made a disposition of his property or a proposal¹⁶⁰ or has applied for a summary instalment order,¹⁶¹ the debtor or the trustee or any creditor may apply to the court¹⁶² and the court may make any of the orders set out in section 41(3). These are:¹⁶³

- (a) order that the disposition or proposal is not an act of bankruptcy;
- (b) halt or refuse the application for adjudication;
- (c) order that any other application for adjudication must not be filed;
- (d) make any order as to costs that the court thinks appropriate; or
- (e) if it orders that costs must be paid to the creditor who has applied for adjudication, order that the costs must be paid out of the debtor's estate.

It therefore seems that bankruptcy procedures will not in all instances take preference over statutory alternative procedures.¹⁶⁴

creditors in this regard. Heath notes that this principle ties in with the 'user pay' principle that New Zealand has adopted through their financial deregulation; Heath 1999 *Osg Hall LJ 422*.

¹⁵⁷ If the adjudication is annulled on the last three grounds the annulment takes effect from the date of the order of annulment; ss 309(3)(b) and 310(4)(b). See par 6.4 as regards statutory compositions.

¹⁵⁸ S 311(1).

¹⁵⁹ S 311(2).

¹⁶⁰ See par 6.5.1.

¹⁶¹ S 41(1). See par 6.5.2. The section does not mention the no asset procedure discussed in par 6.5.3.

¹⁶² S 41(2).

¹⁶³ However, s 41(4) provides that the section does not limit the court's powers under s 37.

¹⁶⁴ See ch 3 par 3.3.2.3 and ch 4 para 4.2.5 and 4.3.4 as regards the South African position which illustrate the difficulties that arise when the legislature does not consider the interplay between procedures.

6.4 Statutory compositions

Part 5 subpart 1 of the Act provides for a statutory composition during bankruptcy.¹⁶⁵ The procedure, which is set out in sections 312 to 324, basically makes it possible for a bankrupt to reach a composition with his creditors by means of a specified creditors' vote (and subsequent court approval) whereafter the bankruptcy is annulled. As regards settlement procedures, the sentiment expressed in the *World Bank Report*, namely, that the benefits thereof are mostly illusory, is apt.¹⁶⁶ Josling comments that this measure is rarely used due to its complexity and the fact that it offers little benefit over a discharge in bankruptcy proceedings. He also remarks that extremely few cases have consequently been decided in terms of the procedure.¹⁶⁷

The procedure in the Act does not set out the manner in which the bankrupt should approach creditors, but requires both a preliminary and a confirming resolution by creditors. The preliminary resolution, accepting the terms of the composition, is taken by special resolution.¹⁶⁸ The confirming resolution, rendering the composition effective, must again be confirmed by way of a special resolution¹⁶⁹ and must be passed within a month after the preliminary resolution was taken.¹⁷⁰

¹⁶⁵ Regs 20 and 21 deal with further procedural matters. Compare the proposal procedure which is similarly structured but which is available prior to bankruptcy; par 6.5.1. See also the South African counterpart; ch 3 par 3.4.

¹⁶⁶ *WB Report* 46. See also ch 2 para 2.6.2.1 and 2.7.

¹⁶⁷ Josling 'Alternatives to bankruptcy' 255. For a discussion of compositions see 260–265.

¹⁶⁸ S 312(1). A special resolution is defined in s 3 as 'a resolution of creditors passed in accordance with section 92(1)(b)'. S 92(1)(b) provides that a special resolution is reached when three-quarters in number and value of creditors who attended the meeting and voted on the resolution vote in favour thereof. S 312(2) provides that where there is more than one class of creditors a delay or failure of one class to accept the composition does not prevent another class from accepting same. This is in line with international principles and guidelines as passive creditors should not be able to hinder agreements; ch 2 par 2.7.

¹⁶⁹ S 313(1). The notice of the meeting to pass the resolution must state the terms of the proposal for composition and must be accompanied by an assignee report on the proposal; s 313(3). Creditors may confirm the composition on varied terms on condition that the final terms are at least as favourable to them as those in terms of the preliminary resolution; s 313(2). S 313(4) provides that where the proposal provides for full payment of all creditors whose respective debts do not exceed a certain amount, that class must not be taken into account when calculating the required majority of creditors necessary to confirm the resolution.

¹⁷⁰ S 320(1)(a). In South Africa, only one meeting and creditors' vote are required. The required percentage is similar to the New Zealand requirement, namely 75% in value and number. Unfortunately, the South African procedure allows passive creditors to hinder an agreement as it does not provide that only the votes of those who attend the meeting and vote will be taken into account; ch 3 par 3.4.

However, in order for a composition to be binding it must be approved by the court¹⁷¹ and a composition so approved binds all creditors in respect of their provable debts.¹⁷² Such an approval will further be conclusive as to the validity thereof.¹⁷³ Court approval must take place within one month after the confirming resolution was passed.¹⁷⁴ The bankrupt or the assignee may apply for approval¹⁷⁵ on notice to creditors.¹⁷⁶ An assignee report on the terms of the composition and the bankrupt's conduct must be before court and the court must further entertain creditors' objections.¹⁷⁷ The court must not alter the substance of a composition but may correct formal or accidental errors or omissions.¹⁷⁸

Nevertheless, the court must not accept the composition if it does not provide the same priority to debts than what the Act provides in terms of its bankruptcy provisions.¹⁷⁹ The court may further refuse approval if it considers that:¹⁸⁰

- (a) section 312 or 313 has not been complied with; or
- (b) the terms of the composition are not reasonable or are not calculated to benefit the general body of creditors; or
- (c) the bankrupt is guilty of misconduct¹⁸¹ that justifies the court in refusing, qualifying, or suspending the bankrupt's discharge; or
- (d) for any other reason it should not approve the composition.

As regards the grounds for refusal, Josling is of the opinion that the court has no residual discretion to decline the request for approval as the request must be heeded unless one of the specific grounds for refusal is made out.¹⁸²

¹⁷¹ S 315(1). The South African statutory composition does not require court approval, although the master should certify that the composition has been duly accepted; ch 3 par 3.4.

¹⁷² S 315(2).

¹⁷³ S 315(5).

¹⁷⁴ S 320(1)(b).

¹⁷⁵ S 316(1).

¹⁷⁶ S 316(2).

¹⁷⁷ S 316(3).

¹⁷⁸ S 316(4).

¹⁷⁹ S 315(4). See pt 3 sub-pt 10. See par 6.3.

¹⁸⁰ S 315(3).

¹⁸¹ With reference to case law Josling summarises misconduct as that which prejudices the bankruptcy process; in particular, conduct which interferes with the rights of creditors to participate in a fair and efficient collective debt recovery process. It covers conduct both before and after the adjudication. However, the conduct must have some degree of proximity to the bankruptcy.

He continues to highlight that it overlaps with matters relating to public interest; Josling 'Alternatives to bankruptcy' 262.

¹⁸² *Idem* 261 and authorities cited there.

Once the court has approved the composition, the bankrupt and the assignee must as soon as practicable¹⁸³ execute a deed of composition for putting the proposal into effect and the assignee may apply to court for the confirmation thereof.¹⁸⁴ The court will confirm the deed if satisfied that it conforms to the approved composition and must direct that the deed be entered and filed in court.¹⁸⁵ The court must also annul the adjudication.¹⁸⁶ However, the annulment does not automatically re-vest the bankrupt's property in the bankrupt as is generally the case when a bankruptcy has been annulled save where the composition provides therefor.¹⁸⁷ On confirmation of the deed and the subsequent annulment, all creditors are bound in all respects as if they had each executed the deed and the bankrupt's property to which the deed refers shall generally vest and must be dealt with in accordance with the deed.¹⁸⁸ A failure to keep to the deadlines as set out in the procedure has the effect that the bankruptcy proceedings resume immediately after such expiry as if there had not been a confirming resolution.¹⁸⁹

As soon as practicable after the deed has been entered, the assignee must take all necessary steps to have any vesting that is provided for therein, registered or recorded in the appropriate registry or office and must thereafter return the deed to

¹⁸³ S 120(1)(c) provides that the bankrupt must execute the deed within five working days after the composition was approved by the court or within additional time if the court has allowed therefor.

¹⁸⁴ S 317(1). No such requirements are found in the South African statutory composition procedure; ch 3 par 3.4.

¹⁸⁵ However, the deed must not be entered and filed in the court unless the assignee's prescribed commission has been paid; s 317(3). The registrar is responsible for entering the deed of composition and must endorse on the deed that it has been entered and filed in court whereafter it must deliver the deed to the assignee if requested to do so; s 321(1).

¹⁸⁶ S 317(2). In South Africa, the sequestration order is not annulled or set aside following a statutory composition, but the insolvent may in some instances apply for an early rehabilitation; ch 3 par 3.4.

¹⁸⁷ S 317(4) read with s 318(b). See par 6.3.4 and compare s 311(1). The re-vesting of property is one of the reasons why South African insolvents attempt to reach statutory compositions. However, the composition must also specifically provide therefor; ch 3 par 3.4.

¹⁸⁸ S 318. This is subject to the provisions of the Land Transfer Act 1952. S 319(1) provides that a bankrupt who makes a composition with creditors, remains liable for the unpaid balance of debt if he, through fraud, incurred or increased the debt or on or before the date of the composition obtained forbearance thereon and the defrauded creditor has not agreed to the composition. S 319(2) provides that a creditor does not agree to the composition by proving the debt and accepting payment of a distribution of the estate's assets.

¹⁸⁹ S 320(2)(a). None of the periods provided for in s 320(1) will in such instances be taken into account in the calculation of a period of time in terms of the Act; s 320(2)(b). The fact that bankruptcy proceedings merely continue if the process is not followed through, is in line with international principles and guidelines that informal procedures should be backed by formal procedures where they fail; ch 2 par 2.7.

the court file.¹⁹⁰ The assignee must further, as soon as practicable, give possession to the bankrupt or the trustee under the composition (as the case may be) of the bankrupt's property or so much thereof as the assignee possesses and that reverts in the bankrupt or trustee under the composition.¹⁹¹

The composition is strengthened by the provision that the court may on application of an aggrieved person, order that default be remedied and may also, on application of an interested person, enforce the provisions of a composition approved by court.¹⁹² Further, after the preliminary resolution has been obtained, the court has exclusive jurisdiction in relation to the composition and the deed of composition as well as the administration thereof.¹⁹³ The subpart finally provides that the law and practice in bankruptcy applies to the deed and that the court must, if relevant, decide a question arising thereunder in accordance therewith.¹⁹⁴

6.5 Alternatives to bankruptcy: Statutory procedures

6.5.1 Proposals

Proposals¹⁹⁵ are regulated in part 5 subpart 2 of the Insolvency Act which consists of sections 325 to 339.¹⁹⁶ Regulations 22 to 43 provide for further procedural matters. This measure also takes the form of a compromise and may be used by an insolvent debtor as an alternative to bankruptcy.¹⁹⁷ Thus, where the statutory composition may be utilised after adjudication, the proposal may be used to escape the consequences of bankruptcy.¹⁹⁸ The process is set in motion when an insolvent makes a proposal

¹⁹⁰ S 321(2)(a).

¹⁹¹ S 321(2)(b).

¹⁹² S 322.

¹⁹³ S 323(1). The court may on application in relation to the composition, the deed or the administration thereof summons and examine the bankrupt and witnesses as if it were bankruptcy proceedings (see pt 3 sub-pt 5). The court may also make orders that it deems appropriate which may include an order in relation to the costs of administration; s 323(2).

¹⁹⁴ S 324.

¹⁹⁵ Proposals were first introduced in the Insolvency Act 1967.

¹⁹⁶ For a discussion of proposals see Josling 'Alternatives to bankruptcy' 265–275.

¹⁹⁷ S 325(1) provides that 'debt' has the same meaning as provable debts in bankruptcy and that an 'insolvent' is a person who is unable to pay his debts as they become due, but excludes a bankrupt. It is thus clear that a person under bankruptcy cannot make use of this procedure. As regards the nature of the procedure the hesitancy of the World Bank to support settlement procedures is reiterated; *WB Report* 46. See also ch 2 para 2.6.2.1 and 2.7.

¹⁹⁸ Compare the proposed South African pre-liquidation composition as contained in cl 118 of the 2015 Insolvency Bill; ch 5 par 5.2.

to creditors for the payment or satisfaction of his debts.¹⁹⁹ Such proposals may include various schemes such as²⁰⁰

- (a) an offer to assign all or any of the insolvent's property to a trustee for the benefit of the creditors;
- (b) an offer to pay the insolvent's debts by instalments;
- (c) an offer to compromise the insolvent's debts at less than 100 cents in the dollar;
- (d) an offer to pay the insolvent's debts at some time in the future;
- (e) any other offer for an arrangement for the satisfaction of the insolvent's debts.

The proposal may also include other conditions that would benefit creditors and may be accompanied by a charge or a guarantee.²⁰¹

The offer must be made in the prescribed form accompanied by a statement of affairs²⁰² and must be signed by the insolvent.²⁰³ It should further recommend a person who is willing to act as trustee for creditors²⁰⁴ and include a statement by such person indicating his willingness to act as such.²⁰⁵ The proposal must be filed in the office of the court²⁰⁶ nearest to the place where the insolvent lives.²⁰⁷ As from the moment that the proposal was filed in court up to the time that the court and creditors have made a decision on the matter, the insolvent may not withdraw the proposal or a charge or guarantee tendered in therewith save with the permission of the court.²⁰⁸

¹⁹⁹ S 326(1).

²⁰⁰ S 326(2).

²⁰¹ S 326(3).

²⁰² S 327(1). S 327(2) provides that the statement of affairs must include the following information:

(a) the insolvent's assets, debts, and liabilities;

(b) the name, address, and occupation of each of the insolvent's creditors;

(c) the securities (if any) held by each creditor.

²⁰³ S 327(3)(a).

²⁰⁴ S 327(3)(b).

²⁰⁵ S 327(3)(c).

²⁰⁶ The proposal's proposed South African counterpart, namely the pre-liquidation composition, will not be reliant on the courts; ch 5 par 5.2. International principles and guidelines favour reduced court involvement; ch 2 par 2.7.

²⁰⁷ S 328(1). The moment the proposal is filed is the moment when creditors' claims are determined; s 328(3). The fact that the proposal must be filed at a court nearest to the insolvent is practical. This is in contrast with the proposed pre-liquidation composition procedure in South Africa where it is suggested that creditors' domiciles are to be followed; ch 5 par 5.2.

²⁰⁸ S 328(2).

The person nominated in the proposal becomes the provisional trustee²⁰⁹ and must as soon as practicable after the proposal is filed call a meeting of creditors to vote on the proposal.²¹⁰ A creditor who has proved a claim²¹¹ may vote by sending a postal vote²¹² to the trustee before or at the meeting²¹³ which has the same effect as if he had been present and voted at the meeting.²¹⁴ The provisional trustee will by default chair the meeting²¹⁵ and creditors may examine the insolvent;²¹⁶ accept the proposal as is or with amendments or modification; and confirm the provisional trustee as trustee or appoint another to the position.²¹⁷ Three-quarters in value and the majority in number of creditors must accept the proposal²¹⁸ and creditors may include, with the insolvent's consent, terms for supervision of the insolvent's affairs.²¹⁹

Once the proposal has been accepted²²⁰ the trustee must as soon as practicable apply to court for an approval and inform the insolvent and creditors of the hearing.²²¹ The court must entertain creditor objections before approving the proposal.²²² The ultimate decision lies with the court and the Act provides guidance as to its discretion. In this regard it provides that the court may refuse the approval in instances where the provisions of the Act have not been heeded; where the terms are not reasonable or calculated to benefit the general body of creditors; or if for any

²⁰⁹ S 329.

²¹⁰ S 330(1).

²¹¹ See reg 31 that specifies that creditors whose claims have been admitted may vote at meetings.

²¹² Reg 34 provides that the postal vote must be in accordance with form 3 of the schedule.

²¹³ S 330(2).

²¹⁴ S 330(3).

²¹⁵ S 331(1).

²¹⁶ See reg 27 regarding the insolvent's obligation to attend meetings.

²¹⁷ S 331(2). Creditors may under certain circumstances appoint a new trustee and the courts may replace a trustee on application by the insolvent or a creditor; reg 42.

²¹⁸ S 331(3). The values are determined on creditors who vote and are personally present or represented or who have casted a postal vote. Reg 26 provides that two creditors constitute a *quorum* and that a creditor is regarded as being present for these purposes if he has voted by postal vote in accordance with s 330(2). If no *quorum* could be constituted the proposal is deemed not to be accepted. International principles and guidelines suggest that passive creditors should not be able to hinder agreements; ch 2 par 2.7. Therefore, the fact that the percentages and number will be calculated having regard to only those who are present and who vote at the meeting is in line with international guidelines. The proposed South African pre-liquidation composition procedure at present suggests a majority in number and two-thirds in value vote of creditors that actually vote; see ch 5 par 5.2.

²¹⁹ S 331(4).

²²⁰ The resolution accepting the proposal must be in the form of a statement including the information set out in reg 22.

²²¹ S 333(1). See also reg 23.

²²² S 333(2).

reason it is not expedient to be approved.²²³ In contrast, the Act provides that the court may not approve a proposal where debts that have priority in bankruptcy are not given equal priority in terms of the proposal²²⁴ and similarly, where priority to trustee's fees²²⁵ and expenses duly incurred in respect of the proposal as well as costs incurred in organising and conducting a meeting of creditors to vote on the proposal have not been heeded.²²⁶ Josling comments that it could be deduced from the wording of section 333 that, where none of the grounds on which a court may decline a proposal is established, the court must approve the proposal as it has no 'residual discretion to decline'.²²⁷ It is important to note that although the court may correct formal or accidental errors or omissions it cannot substantially alter the proposal.²²⁸

If the court approves the proposal, it binds all creditors whose debts are provable and are affected²²⁹ and such approval is conclusive of the validity thereof.²³⁰ Furthermore, a creditor whose debt is provable may not, after the approval and whilst the proposal remains in force, and without the court's permission take steps to file for the insolvent's adjudication, proceed with a creditor's application for adjudication, enforce a civil remedy against the person of the insolvent or his property, or commence any legal proceedings in respect of the debt.²³¹ Once the

²²³ S 333(3). It can be deduced from the word *may* that the court does have the discretion to approve the proposal even where one of the grounds on which the proposal may be declined is made out; Josling 'Alternatives to bankruptcy' 269.

²²⁴ However, this prohibition does not apply where a creditor has waived his right to a priority claim; s 333(5).

²²⁵ Trustees' fees are regulated in reg 40. It provides that the trustee is entitled to a fee, in addition to his reasonable expenses, for work after acceptance of the proposal. It must be paid at the following rates on the net value of property realised after moneys paid to secured creditors in respect of the proceeds of their securities have been deducted:

(a) 20% of the first \$3,000 or part of it, with a minimum of \$200;

(b) 10% of the next \$7,000 or part of it;

(c) 5% of any amount in excess of \$10,000.

²²⁶ S 333(4). In contrast with international guidelines, the procedure does not specifically provide for costless assistance to those who cannot afford it and it also does not specifically provide for legal aid or counselling; ch 2 par 2.7.

²²⁷ Josling 'Alternatives to bankruptcy' 269.

²²⁸ S 333(6). It is for exactly this reason that the procedure cannot be compared with the South African secondary measures; ch 4 para 4.2 and 4.3.

²²⁹ S 334(1). Josling remarks that secured creditors may vote, but that they are generally unaffected by a proposal – although the position is not entirely clear; Josling 'Alternatives to bankruptcy' 273.

²³⁰ S 334(2).

²³¹ S 335. This position is in contrast with international principles and guidelines that favour the position where a moratorium commences the moment an application is filed in order for

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proposal is approved, the insolvent must do everything necessary to put the proposal into effect.²³² The trustee must also at such time take control of property subject thereto, administer and distribute such property accordingly and generally give effect to the proposal.²³³ The trustee must further file with the registrar six-monthly summaries of receipts and payments.²³⁴ He must also attend and report to creditors at creditors' meetings.²³⁵

Even though creditors may not apply for the debtor's adjudication without the court's consent whilst the proposal remains in force,²³⁶ the insolvent may file such an application which will effectively cancel the proposal.²³⁷ The court may further, on application by the trustee or a creditor, vary or cancel the proposal or declare the insolvent bankrupt if satisfied that one or more of the following grounds are applicable:²³⁸ where the insolvent's statement of affairs did not substantially set out the true position or the insolvent gave wrong or misleading replies at his examination which resulted in the acceptance of the proposal that would unlikely have been accepted if the true situation were disclosed; where the insolvent has failed to carry out or comply with the proposal's terms; where, if the proposal proceeds, the creditors will generally suffer injustice or undue delay; or if for any other reason it should be varied or cancelled.²³⁹

negotiations to proceed without an immediate threat of enforcement; ch 2 par 2.7. The proposed pre-liquidation composition in South Africa suggests that a moratorium should become effective once a date for the hearing has been determined; ch 5 par 5.2.

²³² S 336.

²³³ S 337(1). The property must be sold in accordance with the terms of the proposal if a method has been specified therein or where no such method has been determined, in accordance with sch 1; s 337(2). Sch 1 sets out the assignee's general powers which, amongst others, detail the manner in which property should be sold.

²³⁴ S 338. The assignee's summary of receipts and payments as well as his accounts and records are, in the discretion of the registrar, auditable; regs 37 and 38.

²³⁵ Reg 29.

²³⁶ S 335(2) and 335(3).

²³⁷ S 339(5). This element is in line with international guidelines as the possibility of formal proceedings where informal ones fail theoretically enhances the probability of its success; ch 2 par 2.7.

²³⁸ S 339(1) and 339(2).

²³⁹ Generally all property vested in the trustee and which were not sold or disposed of vests, without the necessity for conveyance, transfer or assignment, in the insolvent or where the court adjudicates the insolvent bankrupt, in the assignee; s 339(3). Furthermore the cancellation of the proposal (or cancellation and adjudication) does not prejudice or affect the validity of a contract, sale, disposition, or payment duly made or anything duly done whilst the proposal was in force; s 339(4).

Brown criticises the procedure due to the lack of a moratorium prior to court approval and adds that the necessity of a significant majority of creditors' consent and the involvement of the courts further constitute major disadvantages. He also states that the nature of proposals acceptable to creditors means that they would not be suitable for most debtors with no or few assets.²⁴⁰

6.5.2 Summary instalment orders

Summary instalment orders are regulated by part 5 subpart 3 of the Act which consists of sections 340 to 360.²⁴¹ Further procedural issues are regulated by regulations 44 to 64. This procedure, which in essence constitutes a repayment plan,²⁴² is rather uncomplicated and inexpensive as it does not involve the courts.²⁴³ The debtor or a creditor,²⁴⁴ with the debtor's consent, may apply to the assignee for such an order.²⁴⁵ The order is made by the assignee who may order the debtor to pay debts in instalments (or otherwise), either in full or to the extent that it is considered practical in the circumstances.²⁴⁶ The procedure generally runs for a period of three years²⁴⁷ and may be extended to five years under special circumstances.²⁴⁸

Application should take place in the prescribed form and if the debtor is the applicant, should include extensive information, such as whether the debtor proposes to pay creditors in full or otherwise; details pertaining to the payment; the

²⁴⁰ Brown 'The financial health benefits of a quick "NAP" – New Zealand's solution to consumer insolvency?' 8. Although the proposed pre-liquidation composition in South Africa is intended to provide assistance to NINA debtors, it is submitted that it will not, in its current form and for reasons set out in ch 5 par 5.2, reach its goal.

²⁴¹ For a discussion of summary instalment orders see Josling 'Alternatives to bankruptcy' 275–277. Summary instalment orders were first introduced by the Insolvency Act 1967.

²⁴² Compare the South African repayment plan procedures, namely, the administration order procedure and the debt review procedure; ch 4 para 4.2 and 4.3.

²⁴³ This is in line with international principles and guidelines; ch 2 par 2.7. Both the South African repayment plan procedures are heavily reliant on the courts; *ibid*.

²⁴⁴ Neither of the two South African repayment plan procedures provides for creditors' applications; ch 4 para 4.2 and 4.3.

²⁴⁵ S 341. See further reg 44 regarding the application for a summary instalment order. The application fee is set at NZ\$ 100; reg 44(5).

²⁴⁶ S 340. A discharge is in accordance with international principles and guidelines; ch 2 par 2.7. Both the South African repayment plan procedures require full payment of outstanding debt; ch 4 para 4.2 and 4.3.

²⁴⁷ A three-year period is in line with international principles and guidelines; ch 2 par 2.7.

²⁴⁸ S 349. Neither of the two South African repayment plan procedures provides for a maximum time frame; ch 4 para 4.2 and 4.3.

proposed supervisor²⁴⁹ or reasons why such supervision will not be necessary; and particulars relating to the debtor; his property; creditors; debts; earnings; and employment.²⁵⁰ The assignee may make the order if the total amount of unsecured debt²⁵¹ that is provable in bankruptcy, excluding student loans, adds up to NZ\$40 000²⁵² or less and the debtor cannot immediately repay the debt.²⁵³ The Act does not prescribe factors or circumstances that the assignee should take into account when considering whether to grant the order. The assignee may make

²⁴⁹ A supervisor is defined in s 3 as 'a person who is appointed under section 345'. See below as regards s 345. In South Africa, administrators act as intermediaries in terms of the administration order procedure and debt counsellors in terms of the debt review procedure; ch 4 par 4.2 and 4.3.

²⁵⁰ S 342. See also reg 44.

²⁵¹ Secured credit is included in the South African debt review procedure although the administration order procedure generally excludes same; ch 4 para 4.2 and 4.3. The exclusion of secured debt is in line with international principles and guidelines; ch 2 par 2.7.

²⁵² The summary instalment order will not be invalid if the total amount of debts proved is more than the specified amount. However, in such an instance the supervisor may refer the matter to the assignee who may cancel the order if it deems it appropriate to do so; s 343(3). The amount of NZ\$40 000 may be varied by the Governor-General by Order in Council to bring it in line with increases in the all groups index number of the CPI; s 343(4). In South Africa, the debt review procedure does not contain a maximum monetary threshold as an entry requirement, although the administration order procedure does make such provision in the amount of R50 000. With regard to the exchange rate (see ch 1 par 1.6), the New Zealand threshold clearly provides better access than the South African administration order procedure. Furthermore, Keeper refers to statistics in relation to reasons for rejection of no asset applications in New Zealand and reaches the conclusion that there does not seem to be any significant pressure to increase the threshold; Keeper 2014 *QUT Law Review* 89. Unfortunately detailed statistics as to the reason for the rejection of repayment plan applications are not available in South Africa.

²⁵³ S 343(1). The liquidation test is in line with international guidelines; ch 2 par 2.7. If the debtor or a creditor wants to make representations, the assignee must allow them to do so before making the order; s 343(2). This must be done within ten working days after the date of the notice of application for the order in terms of reg 45; reg 46. Although international principles favour the exclusion of creditor participation as a matter of course, except where the estate represents significant value, the mentioned provisions are better than those in relation to the South African repayment plan procedures where creditor participation constitutes the rule rather than the exception; ch 2 par 2.7 and ch 4 para 4.2 and 4.3. Once the order is made all instalments payable thereunder must be paid in the prescribed manner; see s 351 and reg 62. The debtor, a creditor or the supervisor may at any time apply to the assignee for a variation or a discharge of the order and the assignee may in such instances make an order that it deems appropriate; s 350. See also regs 57 and 58. This feature coincides with international principles and guidelines; ch 2 par 2.7. In South African law, the administration order procedure provides for a variation thereof, but the debt review procedure does not include a similar provision; ch 4 para 4.2 and 4.3.

additional orders regarding future earnings or income, the disposal of goods²⁵⁴ and the powers of the appointed supervisor – if a supervisor is appointed.²⁵⁵

As can be deduced from the discussion above, a suitable and willing supervisor should generally be appointed to supervise the debtor's compliance with the order.²⁵⁶ However, the assignee may dispense with the appointment in appropriate circumstances.²⁵⁷ The order in relation to the supervisor's powers includes the power to direct the debtor's employer to pay all or some of the debtor's earnings to the supervisor²⁵⁸ and to supervise payment of the reasonable living expenses of the debtor and his relatives and dependants.²⁵⁹ The supervisor must supervise the debtor's compliance with both the summary instalment order and additional orders²⁶⁰ and may charge the debtor for his services.²⁶¹ He must, if so requested, provide the assignee with documents relating to the debtor's property, conduct or dealings that

²⁵⁴ This is in line with international principles which provide that non-exempt assets and net earnings should be used to service debt during the period that a debtor is subject to a repayment plan procedure as he should do the best that he can to be rewarded with the discharge at the end of the term; ch 2 par 2.7. The South African debt review procedure does not explicitly provide for an order in terms of which goods should be sold to service debt, although the administration order procedure does provide therefor; ch 4 par 4.2 and 4.3.

²⁵⁵ S 344.

²⁵⁶ S 345(1). He should, amongst others, notify creditors of the summary instalment order; s 353. The notice must be sent within 15 working days of the order being made; reg 47.

²⁵⁷ If a supervisor is not appointed, the provisions of the Act in relation to summary instalment orders apply as if the debtor was the supervisor save for the provisions of s 346 (see below) which will apply as if the assignee was the supervisor; s 345(2). In the event that a supervisor is appointed, the assignee may require him to provide a bond to secure the performance of his obligations under the Act. The assignee must in such circumstances specify the amount of the bond and the person to whom it must be given; s 345(3).

²⁵⁸ These amounts are recoverable as a debt from the employer and the supervisor's receipt is a complete discharge to the employer for such debt; s 357(2). Payment by the employer in contravention of the direction will only discharge the employer if made with the consent of the supervisor or the assignee or to a person other than the debtor who has a stronger legal claim to the money than the debtor; s 357(3). See also reg 55 in relation to the notice to the employer to pay the debtor's earnings to the supervisor. In South Africa, the administration order procedure specifically provides for an emoluments attachment order. However, the debt review procedure does not provide therefor. Also, payments in terms of a debt review order are distributed by payment distribution agencies; ch 4 para 4.2 and 4.3.

²⁵⁹ S 344.

²⁶⁰ S 346(1). The supervisor must, amongst others, notify the assignee and creditors upon the debtor's default in terms of the order; reg 56. See also reg 59.

²⁶¹ S 346(2). The fees may be regulated by the Governor-General by Order in Council; s 346(3). Reg 64 provides that the supervisor may charge the debtor 7.5% of the value of the debtor's assets recovered by the supervisor. It is interesting that, as is the case in South Africa, the procedure does not make mention of a contribution by credit providers as regards costs – as is suggested by international principles and guidelines; see ch 2 par 2.7 read together with ch 4 para 4.2 and 4.3.

are in his possession or under his control.²⁶² His appointment may be terminated by the assignee for failure to supervise the debtor's compliance adequately. In such instances the assignee may appoint a new supervisor.²⁶³

Once the order has been granted, a creditor may not commence or continue proceedings²⁶⁴ unless the permission of the assignee has been obtained or the debtor is in default under the order.²⁶⁵ The debtor's name will be included in a public register of debtors subject to summary instalment orders.²⁶⁶ Money paid by the debtor will be distributed by the supervisor firstly to pay administration costs, then the costs and fees of the assignee, thirdly debts in accordance with the order²⁶⁷ and if a surplus remains, it must be paid to the debtor.²⁶⁸ Once these liabilities have been paid in full, the debtor is discharged from unsecured debts to which the order relates.²⁶⁹ In the absence of evidence to the contrary, there is a presumption that a debtor who defaults under the order has been able to pay and has refused or neglected to do so.²⁷⁰ Once a debtor is in default, enforcement proceedings may begin or continue, unless a district court orders otherwise.²⁷¹ The debtor commits an

²⁶² S 347. See also reg 60 in that the assignee may require the supervisor, or where appropriate the debtor, to render accounts.

²⁶³ S 348. The debt review procedure in South Africa lacks details as regards non-compliant debt counsellors; ch 4 par 4.2.

²⁶⁴ Proceedings are defined in s 352(1) as against the person or property of the debtor in respect of a debt that has been-

- (a) shown in the debtor's application for the summary instalment order;
- (b) included in the summary instalment order; or
- (c) notified to the supervisor.

²⁶⁵ S 352(2). International principles and guidelines suggest that a moratorium should become effective once an application is filed; ch 2 par 2.7. The question as to when a moratorium becomes effective is especially controversial as regards the debt review process in South Africa; ch 4 par 4.3.

²⁶⁶ S 354. The assignee must maintain a register of persons subject to a current order. An order is not current when discharged or instalments have been paid in accordance therewith; s 355.

²⁶⁷ Generally payments to creditors should take place every four months; reg 63(1). In South Africa, although not specifically required or necessary in terms of the debt review procedure, it is generally expected that payments are effected on a monthly basis. The administration order procedure prescribes that payments are made every three months; ch 4 para 4.2 and 4.3.

²⁶⁸ S 358(1). Reg 18(2) provides that the assignee's rate of remuneration is 2.5% of the value of the debtor's assets recovered by the supervisor. See ch 4 para 4.2 and 4.3 in relation to administrators' and debt counsellors' fees.

²⁶⁹ S 358(2). The supervisor must provide the assignee with a statement of receipts and payments subsequent to the discharge of the order; reg 61.

²⁷⁰ S 359(1).

²⁷¹ S 359(2). The supervisor must as soon as practicable notify the assignee of a debtor's default in terms of the order; s 359(3). In South Africa, an administration order may be rescinded in the event that the debtor defaults thereon where after credit providers may institute enforcement

Footnote continues on next page

offence if he obtains credit, incurs a liability or enters into a hire purchase agreement of NZ\$1 000 or more.²⁷² However, it will be a defence to the first two offences if the debtor informed the person extending the credit or to whom the liability was incurred that he was affected by a summary instalment order.²⁷³

6.5.3 No asset procedure

The no asset procedure is provided for in part 5 subpart 4 of the Insolvency Act which consists of sections 361 to 377B.²⁷⁴ Regulations 65 to 68 deal with supplementary procedural matters. The procedure was first introduced by the present Act and offers a debt relief procedure to a debtor 'who has no realisable assets' and 'does not have the means of repaying any amount towards those debts'.²⁷⁵

Josling summarises the policy behind the procedure in that²⁷⁶

the full bankruptcy process, with its duration, and consequential restrictions, is no longer appropriate to most small debtors. These debtors, it is said, are typically always struggling to pay their debts, and are usually pushed into bankruptcy by some unfortunate event. In bankruptcy, a dividend is hardly ever paid to creditors. Thus the justifications combine economic, humanitarian, and practical rationales.

It therefore seems that one of the major driving forces behind the introduction of the no asset procedure was the need to channel assetless insolvents towards a more appropriate debt relief measure, as they previously mainly opted for bankruptcy

procedures. Under the debt review procedure creditors may, without more, institute enforcement proceedings once a debtor defaults in terms of a debt review order; ch 4 para 4.2 and 4.3.

²⁷² S 360(1). Offences under this section are punishable by imprisonment for a term not exceeding one year or a fine not exceeding NZ\$5 000 or both; s 360(3).

²⁷³ S 360(2).

²⁷⁴ For a discussion of the no asset procedure see Josling 'Alternatives to bankruptcy' 278–282 and Keeper 2014 *QUT Law Review* 79.

²⁷⁵ S 361 and s 363(1)(a) and (e). The fact that the New Zealand insolvency system makes specific provision for NINA debtors is on par with international principles and guidelines in that discrimination on financial grounds is avoided and as provision is made for debtors' differing circumstances and merits; ch 2 par 2.7. Compare cl 118(22) of the 2015 Insolvency Bill, which sets out the second part of the procedure as provided for in the proposed pre-liquidation composition in South Africa which is intended as a solution to NINA debtors' plight; ch 5 par 5.2. The proposal is on the table since none of the statutory debt relief measures in South Africa provides for this group at present; see chs 1, 3 and 4. See also Coetzee and Roestoff 2013 *Int Insolv Rev* where the argument that the New Zealand no asset procedure may constitute a model for South Africa originated.

²⁷⁶ Josling 'Introduction' 7. See further Keeper 2014 *QUT Law Review* 85–87.

which is not suited to their needs.²⁷⁷ Guest refers to the belief that the no asset procedure will have a considerably reduced amount of social stigma attached to it.²⁷⁸

A debtor can secure entry to the procedure on application to the assignee²⁷⁹ by completing and filing an application form and a statement of affairs.²⁸⁰ Given the fact that the no asset procedure remains for a twelve-month period, as opposed to the three-year period under bankruptcy, parliament has set up strict entry criteria in order to prevent abuse.²⁸¹ The criteria can be divided into criteria relating to the debtor's objective financial position and those relating to his conduct. The assignee may admit or refuse the debtor to the procedure depending on its satisfaction that the criteria have been met on reasonable grounds.²⁸² The financial requirements are that the debtor has no realisable assets²⁸³ and that the total debt is not lower than NZ\$1 000 and not more than NZ\$40 000.²⁸⁴ The debtor must further not have the means of repaying any amount towards such debts.²⁸⁵ Further criteria are that the

²⁷⁷ See Brown and Telfer *Personal and corporate insolvency legislation* 37. The situation differs from the South African system where NINA debtors are practically excluded from the sequestration procedure. These debtors also do not presently have access to any of the secondary debt relief measures; chs 3 and 4.

²⁷⁸ Guest 'Introduction: Personal insolvency' 18.

²⁷⁹ Courts are not involved in the procedure which is in line with international principles and guidelines; ch 2 par 2.7.

²⁸⁰ S 362(1) and 362(2). Refer also to reg 65. S 362(3) provides that the assignee may reject the application if such application or the statement of affairs is according to the assignee incorrect or incomplete.

²⁸¹ See Brown and Telfer *Personal and corporate insolvency legislation* 38.

²⁸² S 363(1).

²⁸³ S 363(1)(a) – that is the requirement relating to the debtor's solvency position. S 363(2) provides that realisable assets do not include those assets that a bankrupt is allowed to retain under s 158, but does include assets that the assignee may recover if the debtor were adjudicated bankrupt and if the irregular transaction provisions in terms of sub-pt 7 of pt 4 applied. The subsection was amended to its current form by s 7 of the Insolvency Amendment Act 2009; see Keeper 2014 *QUT Law Review* 93–94 as regards amendments.

²⁸⁴ S 363(1)(d). S 363(3) provides that these amounts may be altered by the Governor-General by Order in Council to take cognisance of the CPI. The proposed pre-liquidation composition procedure in South Africa contains a suggested monetary threshold of R200 000; ch 5 par 5.2. See ch 1 par 1.6 as regards the exchange rate.

²⁸⁵ S 363(1)(e) – this requirement relates to liquidity. Such determination is made under a prescribed means test. See reg 66 which provides that:

The prescribed means test for the purposes of section 363(1)(e) is whether, taking into account the income of the debtor personally and that of any relative with whom the debtor lives, the debtor has a surplus of money after paying the household's usual and reasonable living expenses.

Keeper mentions that actual guidelines used by the assignee are not regularly available and that, with reference to the budget form on the government website, the question seems to be whether the debtor has any net disposable income available. She also comments that the procedure is predominately for the unemployed; Keeper 2014 *QUT Law Review* 89–90. However, Footnote continues on next page

debtor should not previously have been admitted to the no asset procedure²⁸⁶ or have been adjudicated bankrupt.²⁸⁷ As far as the debtor's conduct is concerned, he is disqualified from entry and the assignee must not admit him to the no asset procedure

- a. if he has concealed assets with the intention to defraud creditors;²⁸⁸
- b. if he has engaged in conduct that would constitute an offence under the Act if he was adjudicated bankrupt;²⁸⁹
- c. if he has incurred debt or debts whilst knowing that he does not have the means to repay such debts;²⁹⁰ or
- d. where a creditor intends to apply for his adjudication as a bankrupt and there is a likelihood that the outcome will be materially better than under the no asset procedure.²⁹¹

The assignee must, as soon as practicable after the debtor has applied for entry, send a summary of the debtor's assets and liabilities to all known creditors.²⁹² Once the application has been made, a debtor must not obtain credit of more than NZ\$100 without informing the credit provider that he has applied as such.²⁹³

A debtor is formally admitted to the procedure when the assignee sends a written notice to that effect to the debtor.²⁹⁴ The assignee must also notify creditors and advertise that the debtor has been admitted to the no asset procedure as soon as

international guidelines prefer a standards-based approach supplemented with an element of discretion; ch 2 par 2.7.

²⁸⁶ S 363(1)(b). The fact that a debtor only has one opportunity to make use of the no asset procedure is an attempt to manage the risk of abuse; see Keeper 2014 *QUT Law Review* 86 and authorities stated there.

²⁸⁷ S 363(1)(c).

²⁸⁸ S 364(a).

²⁸⁹ S 364(b).

²⁹⁰ S 364(c). See Brown and Telfer *Personal and corporate insolvency legislation* 41 who express the view that this exclusion may be problematic in that the assignee may have difficulty in applying the disqualification where for instance a debtor in dire circumstances was forced to take out a loan which he honestly believed could be repaid in future even though he does not have the means to repay it immediately.

²⁹¹ S 364(d).

²⁹² S 365.

²⁹³ S 366.

²⁹⁴ S 367(1). Creditors do not participate in the procedure which coincides with the international guideline that creditors should only participate in instances where estates represent significant value; ch 2 par 2.7.

practicable.²⁹⁵ The assignee must further maintain a public register of persons admitted to and discharged from the procedure.²⁹⁶

Creditors, on the other hand, may not begin or continue to recover or enforce debt once a debtor has been admitted to the procedure.²⁹⁷ Debts that may not be enforced are those which were owed on the date of application and would be provable under bankruptcy.²⁹⁸ However, this procedure does not apply to maintenance orders,²⁹⁹ amounts payable under the Child Support Act³⁰⁰ and student loans.³⁰¹

The debtor under the no asset procedure has a number of duties including the duty to comply with reasonable requests by the assignee to provide assistance, documents and other information necessary for applying the procedure to the debtor.³⁰² He must also notify the assignee as soon as possible of a change in circumstances that would allow him to repay an amount towards the debts under the procedure³⁰³ and must not obtain credit of more than NZ\$1 000 without first informing the credit provider that he is subject to the no asset procedure.³⁰⁴ The debtor commits an offence if he obtains credit or incurs a liability or enters into a hire purchase agreement of NZ\$1 000 or more.³⁰⁵ However, it will be a defence to the

²⁹⁵ S 367(2). See also reg 67.

²⁹⁶ S 368(1). The register must be maintained in accordance with pt 7, sub-pt 5; s 368(2). See also s 448(3) and 448(4). S 368(1) was amended by s 13(6) of the Insolvency Amendment Act 2009 to provide for the inclusion of persons who have been discharged from the procedure on the public register. Such entries will remain for a period of four years. The information will thus be kept for a total of five years. Keeper argues that this amendment has diluted the objective of providing debtors with a 'clean slate' and has aligned it more with bankruptcy; Keeper 2014 *QUT Law Review* 93.

²⁹⁷ International guidelines favour the position where a moratorium on debt enforcement commences once an application for debt relief has been filed; ch 2 par 2.7.

²⁹⁸ S 369(1). Secured debts are generally excluded from bankruptcy and therefore also from the no asset procedure; s 243. The exclusion of secured credit tallies with international principles and guidelines; ch 2 par 2.7.

²⁹⁹ Under the Family Proceedings Act 1980.

³⁰⁰ Child Support Act 1991.

³⁰¹ S 369(2). The fact that student loans are enforceable under the no asset procedure is in contrast with bankruptcy where student loans are discharged. Compare ss 369(2)(c) and 304. Although the rationale behind the exclusion of student loans may be questioned, the wide discharge that the procedure offers is in line with international principles and guidelines; ch 2 par 2.7.

³⁰² S 370(1).

³⁰³ S 370(2).

³⁰⁴ S 370(3).

³⁰⁵ S 371(1). Offences under this section are punishable by imprisonment not exceeding one year or a fine not exceeding NZ\$5 000 or both; s 371(3).

first two offences if the debtor informed the person extending the credit or to whom the liability was incurred that he had been admitted to the no asset procedure.³⁰⁶

The procedure can be terminated upon the happening of various events, for example upon the debtor's discharge,³⁰⁷ the debtor's application for his own adjudication³⁰⁸ or the application for adjudication by a credit provider that is entitled to do so.³⁰⁹ The assignee may terminate the no asset procedure where the debtor was wrongly admitted (for example where the debtor concealed assets or misled the assignee)³¹⁰ or where the assignee is satisfied that the financial circumstances have changed to such an extent that the debtor can repay an amount towards his debt.³¹¹ Termination by the assignee takes place by sending a notice to the debtor and becomes effective when the notice is sent, irrespective of whether it is received by the debtor.³¹² The assignee must thereafter also notify known creditors.³¹³ If the assignee terminated the participation on the ground that the debtor has concealed assets or misled the assignee, the court, on application by the assignee, may make a preservation order³¹⁴ on terms and conditions that the court sees fit, pending an application for the debtor's adjudication.³¹⁵ A creditor may apply to the assignee for termination where the creditor objects on grounds that the debtor did not meet the entry requirements³¹⁶ or where there are reasonable grounds for the assignee to conclude that the debtor was disqualified on grounds in terms of section 364.³¹⁷ The first three grounds for disqualification in terms of section 364 relate to dishonesty,³¹⁸ while the fourth ground refers to the situation where a creditor intends to apply for the debtor's adjudication as a bankrupt and the outcome would likely be better under the

³⁰⁶ S 371(2).

³⁰⁷ S 372(b) and s 377.

³⁰⁸ S 372(c).

³⁰⁹ S 372(d). For instance, a credit provider may apply for adjudication where the creditor's claim remains enforceable under a student loan; s 372(d) read together with s 369(2).

³¹⁰ S 372 read together with s 373(1)(a).

³¹¹ S 372 read together with s 373(1)(b).

³¹² S 373(2). See reg 68 regarding the assignee's notice to the debtor.

³¹³ S 373(3).

³¹⁴ To protect or preserve property in the interim for the benefit of creditors; see Guest 'Process for procuring bankruptcy' 57.

³¹⁵ S 374.

³¹⁶ S 376(1) read together with 376(2)(a).

³¹⁷ S 376(1) read together with 376(2)(b).

³¹⁸ The disqualification of debtors who acted fraudulently or have engaged in serious misconduct is in accordance with international principles; ch 2 par 2.7.

bankruptcy procedure than under the no asset procedure as was also mentioned above. It is therefore clear that the bankruptcy avenue will still be available to creditors after the no asset procedure has commenced. If a creditor discovers that bankruptcy may be more beneficial, the creditor may apply to the assignee for termination and apply for the debtor's adjudication as a bankrupt.

Termination of the procedure, except termination by discharge, lifts the moratorium on debt enforcement. The debtor will also be liable to pay penalties and interest that may have accrued whilst the procedure was in force.³¹⁹

If the procedure is not terminated on grounds other than the discharge, the debtor will automatically be discharged from the procedure twelve months after the date on which the debtor was admitted thereto.³²⁰ However, such discharge will not take place where the assignee is satisfied that the twelve-month period should be extended to appropriately consider whether the procedure should be terminated and the assignee has sent a notice of deferral to the debtor.³²¹ The notice³²² must indicate the alternative date for automatic discharge, which must not be more than 25 working days after expiry of the twelve-month period.³²³ The debtor will be automatically discharged on the date stated in the notice.³²⁴ The assignee must also send a written notice of the deferral to known creditors as soon as practicable.³²⁵

Upon discharge, the debtor's debts that became unenforceable are cancelled and the debtor is not liable to pay any part thereof. This includes penalties and interest.³²⁶ The discharge does not apply to debt or liability incurred by fraud or fraudulent breach of trust or for which the debtor has obtained forbearance through

³¹⁹ S 375. The latter sentence was introduced by s 8 of the Insolvency Amendment Act 2009.

³²⁰ S 377(1). The discharge is in accordance with international principles and guidelines and, within the auspices of NINA debtors, in line with the requirement that discrimination on financial grounds should be rooted out; ch 2 par 2.7.

³²¹ S 377(2). S 377(2)–(7) was added by s 9(2) of the Insolvency Amendment Act 2009.

³²² The notice is effective whether the debtor receives it or not; s 377(4).

³²³ S 377(3).

³²⁴ S 377(6). The notice may be revoked, in which case the debtor is automatically discharged on expiry of the twelve-month period – if the notice was revoked prior to that date. If that is not the case, the debtor will be discharged on the date of revocation; s 377(7).

³²⁵ S 377(5).

³²⁶ S 377A(1). S 377A was inserted by s 10(2) of the Insolvency Amendment Act 2009.

fraud.³²⁷ These debts and liabilities become enforceable on discharge and the debtor is also liable for penalties and interest thereon.³²⁸ Finally, the discharge relates to the debtor only and not to business partners, co-trustees, guarantors or any person jointly bound or who had entered into any contract with the discharged debtor.³²⁹

Telfer comments that the difference between the three-year discharge period in bankruptcy and the twelve-month period in the no asset procedure may lead to possible abuse of the no asset procedure in order to ‘fast track’ the discharge. He states that the bigger the inconsistency between the two procedures, the greater the need for resources to ensure that the system is not misused.³³⁰

It is important to refer to a 2011 report by the then Ministry of Economic Development on the evaluation of the procedure.³³¹ The aims of the research were to assess the cost-effectiveness of the procedure in comparison to other options; the impact on users; the reach and uptake of the procedure; and the quality of the scheme administration.³³² The key points that were distilled from the evaluation relate to the outcomes, effectiveness and responsiveness of the procedure. When the outcomes were measured it was established that the procedure is successful in reaching the social and economic objectives thereof and that it is helpful in genuine circumstances of indebtedness by providing a fresh start. It was found that the procedure should remain as an option for over-indebted persons and particularly for ‘no fault’ situations. The effectiveness of the procedure is documented as providing a short-term answer for individuals in severe debt, but it was established that it does not spur the adoption of responsible long-term financial behaviour. It was noted that NGOs and budget advisers have a significant role to play in the operation of the

³²⁷ S 377A(2).

³²⁸ S 377A(3).

³²⁹ S 377B. This section was inserted by s 11 of the Insolvency Amendment Act 2009.

³³⁰ See Telfer ‘New Zealand bankruptcy law reform: The new role of the official assignee and the prospects for a no-asset regime’ 265–266. In this regard, see the discussions in relation to the equality principle within the realm of South African law which basically entails that those who are similarly situated should be similarly treated; ch 1 par 1.1, ch 3 par 3.5 and ch 4 par 4.4. This begs the question as to whether this principle would be applicable to periods under different statutory insolvency procedures. Furthermore, international principles and guidelines caution against the perception that an insolvency procedure provides an easy way out; ch 2 par 2.7.

³³¹ Ministry of Economic Development *Evaluation of the no asset procedure*. See also Keeper 2014 *QUT Law Review* 94–96 where the author comments on the evaluation.

³³² Ministry of Economic Development *Evaluation of the no asset procedure* 2.

procedure and its effectiveness for debtors. Under the heading ‘responsiveness’ it is recognised that the administration of the procedure is very efficient but that it should continue to be developed to meet policy objectives. The refinements should include suitable procedures and initiatives to enable debtors to best deal with their insolvency responsibility and to cultivate decent budgeting practices. It is stated that debtors under the procedure value the service provided by the insolvency and trustee service and that new changes in the service will enhance the on-line application process. It is finally acknowledged that the procedure has unintended consequences (for example that it is misused in some instances) and unplanned costs – which can be reduced.³³³ However, with reference to the misuse of the procedure, Keeper, with reference to statistics, submits that ‘few debtors are attempting to abuse the procedure’.³³⁴ Nevertheless, with reference to relevant statistics and the *WB Report*, she is of the opinion that the procedure does not necessarily change debtors’ attitudes as regard the proper use of credit. She therefore suggests that³³⁵

The brevity of the 12-month NAP procedure and the absence of mandated budgeting or financial literacy course potentially were identified as challenges to the success of NAP in terms of the objective of economic rehabilitation. It is recommended that the NAP be amended to require mandatory participation in such courses as a pre-condition of discharge. The completion of an ‘earned’ fresh start would not only encourage changes in behaviour, but may also increase the legitimacy of NAP in the eyes of society.

6.6 Informal arrangements

Josling refers to two types of compromises that fall outside the statutory framework. These compromises can be used by the debtor prior to bankruptcy as the statutory composition is prescribed after a debtor has been adjudicated bankrupt. These arrangements have the advantages of being more flexible and less expensive than their statutory counterparts. Court involvement is also limited.³³⁶

The first type of compromise is the basic contract in terms whereof a debtor agrees with creditors that he will pay a certain amount towards his debts in full and final

³³³ *Idem* 2–3.

³³⁴ Keeper 2014 *QUT Law Review* 90.

³³⁵ *Idem* 96–97.

³³⁶ Josling ‘Alternatives to bankruptcy’ 282.

settlement. The obvious disadvantage of this procedure is that all creditors must consent thereto, not least because a dissenting creditor could proceed with bankruptcy proceedings, thereby jeopardising the entire arrangement. The second type of compromise takes the form of an 'assignment for the benefit of creditors'. Josling comments that this construction is essentially a 'hive down'³³⁷ for individuals. It essentially entails a debtor assigning his property to a trustee for the benefit of creditors. It may be accompanied by a contract with creditors or not. Again, where there is no agreement by creditors, they are free to discard payments by the trustee and proceed with bankruptcy proceedings.³³⁸ Josling notes that the main advantage of this instrument is that the debtor does not have a beneficial interest in the property after the assignment is complete which will render the possibility of a subsequent bankruptcy of no benefit to creditors. However, section 18 of the Insolvency Act specifically provides that a disposition of property to a trustee for the benefit of creditors constitutes an act of bankruptcy. Other acts of bankruptcy that may arise in the attempt to reach an informal arrangement is that the debtor may notify a creditor that he has suspended or is about to suspend payment of debts³³⁹ or an admission of insolvency under prescribed circumstances.³⁴⁰ As was mentioned on various occasions above, an attempt at settlements will more often than not be unsuccessful.³⁴¹ These constructions also do not feature any of the elements that international principles and guidelines suggest would enhance their chances of success.³⁴²

6.7 Conclusion

The study of the New Zealand system was motivated by mostly two reasons. The first is the system's simplicity and efficiency which was one of the seven planned modifications that the 2006 Act had to bring about.³⁴³ It is especially attractive from a South African perspective where the broader debt relief landscape is devoid of any

³³⁷ Crossland describes a hive-down, which is mainly used in corporate rescues, as an instrument whereby a company sells its more favourable components to a subsidiary in order to preserve and maximise the value of the struggling company. The shares or transferred assets are subsequently sold to a third party; Crossland 'Hiving-down' 349.

³³⁸ Josling 'Alternatives to bankruptcy' 283.

³³⁹ S 22.

³⁴⁰ S 23. Josling 'Alternatives to bankruptcy' 283.

³⁴¹ *WB Report* 46. See also ch 2 para 2.6.2.1 and 2.7.

³⁴² See ch 2 par 2.7.

³⁴³ See par 6.2.

policy objectives and where reform has taken place in an incoherent, piecemeal fashion which has resulted in a multiplicity of government departments, pieces of legislation, policies, procedures, forums, regulators and intermediaries involved which obviously have a hefty price tag attached.³⁴⁴ The second reason is that the system does not discriminate against insolvent individuals on financial grounds and has even introduced a specific procedure for the NINA category of debtors.³⁴⁵ This category is at present totally excluded from the South African system, although it is argued that the group represents the majority of over-committed debtors in the country. The exclusion raises questions and concerns along socio economic and constitutional lines.³⁴⁶

The New Zealand system provides for bankruptcy and alternative statutory measures in the form of proposals, summary instalment orders and the no asset procedure. It also provides for a statutory composition that is available after bankruptcy. It is important to note that the wider personal insolvency system in New Zealand is regulated by a single statute, namely, the 2006 Insolvency Act and that one ministry, namely that of business, innovation and employment is responsible therefor. Also, the assignee is involved in the majority of procedures. This is in contrast with the South African position where multiple ministries, statutes, regulators and intermediaries are involved.³⁴⁷ The New Zealand Insolvency Act's emphasis is seemingly on the humane and supportive treatment of bankrupts which tallies with international principles and guidelines.³⁴⁸ It further appears that public interest constitutes a major consideration and that the assignee acts as the guardian thereof.³⁴⁹ The system clearly attempts, in line with international principles and guidelines, to balance the interests of the debtor, creditors and society at large.³⁵⁰ In the South African system the interest of creditors constitutes the main and overreaching objective of insolvency legislation in general.³⁵¹

³⁴⁴ See chs 3 and 4 in general.

³⁴⁵ Para 6.1 and 6.5.3.

³⁴⁶ See Coetzee and Roestoff 2013 *Intern Insolv Rev* 207–210 and the discussions in ch 1 par 1.1, ch 3 par 3.5 and ch 4 par 4.4.

³⁴⁷ See chs 3 and 4.

³⁴⁸ Ch 2 par 2.7 and par 6.2.

³⁴⁹ Par 6.2.

³⁵⁰ Ch 2 par 2.7.

³⁵¹ See in general chs 3 and 4.

When the New Zealand system is viewed as a whole it, honours the principles that all honest but unfortunate debtors should be able to gain access to statutory debt relief measures which should lead to a discharge of debt³⁵² – unlike the South African position.³⁵³ However, the jurisdiction goes further by acknowledging that not all debt situations are alike and that more than one debt relief option, depending on the debtor’s circumstances, should be available to overcommitted individuals. Another laudable attribute of the broader New Zealand system is the general exclusion of the courts in bankruptcy, summary instalment orders and the no asset procedures where, as was mentioned, the official assignee now oversees all of these procedures.³⁵⁴ This neutral state-funded ‘one stop shop’ is in a unique position to channel debtors towards the most suitable procedure.³⁵⁵ It is prudent to first reflect on this feature as regards the South African position.

It is a non-refutable fact that New Zealand, in line with international principles and guidelines,³⁵⁶ sets an excellent example by generally excluding court involvement from the insolvency process. The South African system stands in stark contrast with this initiative as all of its statutory debt relief measures are heavily reliant on the already over-burdened courts.³⁵⁷ As international principles and guidelines wisely suggest that developing countries should rather build on existing institutions and infrastructure than developing novel ones,³⁵⁸ the alternative South African options need to be considered.

Turning to the specific procedures, the first procedure that was discussed is the New Zealand bankruptcy procedure which can be compared to the South African sequestration procedure.³⁵⁹ Although both systems provide for debtor and creditor applications, in South Africa, both voluntary surrender and compulsory sequestration applications are made to the high court³⁶⁰ where the New Zealand system only

³⁵² Para 6.2, 6.3, 6.4 and 6.5 read with ch 2 par 2.7.

³⁵³ See ch 3 par 3.3 and ch 4 para 4.2 and 4.3.

³⁵⁴ See para 6.2, 6.3 and 6.5.

³⁵⁵ Par 6.2.

³⁵⁶ Ch 2 par 2.7.

³⁵⁷ Ch 3 par 3.3 and ch 4 para 4.2 and 4.3.

³⁵⁸ *WB Report* 60–61 and 131. See also ch 2 par 2.7.

³⁵⁹ Par 6.3 read with ch 3 par 3.3.

³⁶⁰ Ch 3 par 3.3.

requires a court application where creditors apply for adjudication.³⁶¹ In contrast with the South African system which, in both debtor and creditor applications, requires that advantage for creditors be shown, no such statutory requirement is to be found in the New Zealand system, although mention has been made of the possibility that it is indirectly required in creditor applications.³⁶² This is interesting as in South Africa, the onus of proof as regards the advantage for creditors requirement is applied more strictly in voluntary applications than in compulsory sequestration proceedings.³⁶³ The fact that the New Zealand system takes a firmer stand on compulsory applications heeds the warning that creditor applications may be misused.³⁶⁴ Other positive attributes of the New Zealand system from which South Africa could possibly draw and which are in line with international principles and guidelines are the moratorium on debt enforcement once an application is filed and the automatic discharge after a period of three years.³⁶⁵

As regards the property that the debtor may retain, the New Zealand system is limited and does not adhere to international principles and guidelines that favour a standards-based approach where most property are excluded from the estate as a matter of course and where property is only claimed if it represents significant value.³⁶⁶ However, it does provide for the retention of a motor vehicle and the family home at least receives some recognition³⁶⁷ albeit with reference to another piece of legislation.³⁶⁸ Such allowances are foreign to South African insolvency law.³⁶⁹

As far as the interaction between the various statutory procedures is concerned, the Act, in line with the objectives of simplicity and efficiency, clearly sets out the interplay between the different procedures.³⁷⁰ Such procedural consciousness sets

³⁶¹ Par 6.3.1.

³⁶² Par 6.3.2.

³⁶³ Ch 3 par 3.3.2.

³⁶⁴ Ch 2 par 2.7.

³⁶⁵ Ch 2 par 2.7 read with para 6.3.2 and 6.3.4.

³⁶⁶ Par 6.3.3 and ch 2 par 2.7.

³⁶⁷ Par 6.3.3.

³⁶⁸ Joint Families Home Act 1964.

³⁶⁹ Ch 3 par 3.3.3.

³⁷⁰ Par 6.3.5, 6.4 and 6.5.

an example for possible South African reform as the South African system does not adequately address this issue which has created numerous practical problems.³⁷¹

Both the New Zealand and South African systems provide for a statutory composition after bankruptcy/sequestration.³⁷² The statutory composition provided for by the New Zealand Insolvency Act is apparently rarely used due to its complexity and the little benefit that it offers over a discharge in bankruptcy.³⁷³ Save for the fact that the procedure does not allow passive creditors to hinder agreements, it does not have much to offer in relation to its South African counterpart. In any event, the *World Bank Report* suggests that the benefits of settlements are mostly illusory.³⁷⁴

A proposal is the first of three alternative procedures to bankruptcy and shares characteristics of the proposed South African pre-liquidation composition.³⁷⁵ It also takes the form of a compromise, but may be used to escape the consequences of bankruptcy.³⁷⁶ However, once again, the sentiment expressed by the *World Bank Report* that settlement procedures' benefits are mostly illusory, is emphasised.³⁷⁷ Nevertheless, the proposed South African pre-liquidation composition procedure could draw from the New Zealand measure in three respects. The first is the title which is more descriptive and which does not create the impression that its invocation is a pre-liquidation requirement. The second is that no monetary threshold as regards entry is set and the third is that the domicile of the debtor is followed as opposed to that of creditors which is impractical. Although the proposed South African procedure intends to cater for especially the NINA category of debtors,³⁷⁸ which at first glance seems like an advantage over the New Zealand procedure, it has been determined that it will not reach its objective.³⁷⁹

³⁷¹ See ch 3 par 3.3.2.3 and ch 4 para 4.2.5 and 4.3.4 as regards the South African position.

³⁷² See ch 3 par 3.4 and par 6.4.

³⁷³ Josling 'Alternatives to bankruptcy' 255.

³⁷⁴ *WB Report* 46. See also ch 2 para 2.6.2.1 and 2.7.

³⁷⁵ See par 6.5.1 and ch 5 par 5.2.

³⁷⁶ S 325(1).

³⁷⁷ *WB Report* 46. See also ch 2 para 2.6.2.1 and 2.7.

³⁷⁸ See 2014 *Explanatory memorandum* 201 and 208.

³⁷⁹ Ch 5 par 5.2.

The New Zealand summary instalment order procedure can be equated with the South African debt review and administration order procedures as it basically entails a repayment plan that is forced upon parties by a disinterested third party.³⁸⁰ The summary instalment order procedure is uncomplicated and scores high when measured against international principles and guidelines.³⁸¹ Commendable qualities which are lacking in the debt review procedure in South Africa³⁸² is the general time frame of three years; the discharge of unsecured debt at the end of the term and coupled therewith that secured credit is excluded from the procedure; that it provides for the disposal of goods; that creditor participation does not take place as a matter of course; that it specifically provides for a variation of the plan if needs be; that it provides for an emoluments attachment order; and the details as regards non-compliant supervisors.³⁸³ In relation to the South African administration order procedure³⁸⁴ the discharge after a period of three years is of significance.³⁸⁵

Of special importance for South African reform is the New Zealand no asset procedure.³⁸⁶ This is so since South Africa does not provide any form of recourse for the NINA category of debtors which, it was submitted, is unconstitutional.³⁸⁷ Further, NINA debtors presently constitute the majority of insolvent debtors in South Africa.³⁸⁸ Although the second part of the proposed South African pre-liquidation composition³⁸⁹ is supposed to fill this gap,³⁹⁰ it was established that (when implemented) it will not reach this objective.³⁹¹ The proposed procedure, as contained in cl 118(22) of the 2015 Insolvency Bill, is also so sparse that a proper comparison of procedural aspects is not practical.

It is submitted that the structure of the New Zealand no asset procedure is suited to South Africa's needs as it is uncomplicated and inexpensive. Furthermore, the

³⁸⁰ See par 6.5.2 and ch 4 para 4.2 and 4.3.

³⁸¹ Ch 2 par 2.7.

³⁸² Ch 4 par 4.3.

³⁸³ Par 6.5.2.

³⁸⁴ Ch 4 par 4.2.

³⁸⁵ Par 6.5.2.

³⁸⁶ Par 6.5.3.

³⁸⁷ Ch 1 par 1.1, ch 3 par 3.5 and ch 4 par 4.4.

³⁸⁸ Coetzee and Roestoff 2013 *Int Insolv Rev* 189. See also ch 1 par 1.1.

³⁸⁹ Ch 5 par 5.2.

³⁹⁰ See 2014 *Explanatory memorandum* 201 and 208.

³⁹¹ Ch 5 par 5.2.

discharge of NINA debtors' debts is not a new phenomenon in New Zealand and therefore, the introduction of a specific procedure to cater for the unique needs of NINA debtors already constitutes an improvement of debt relief measures as regards this category of debtors in New Zealand. The procedure has also been developed further by means of the Insolvency Amendment Act³⁹² and a study suggests that it is successful in reaching its social and economic objectives.³⁹³ Obviously, no procedure should ever be wholly transplanted from one jurisdiction to another, although national factors should not be over-emphasised.³⁹⁴ Therefore, a consideration of the introduction of the essence of the New Zealand no asset measure must be done, keeping in mind the South African legal and insolvency landscape and perhaps more importantly the realities that a developing country face as regards its existing infrastructure.³⁹⁵ Cognisance should also be taken of the limited instances where the New Zealand no asset procedure does not conform to international principles and guidelines. Furthermore, comments by New Zealand observers should be viewed in a serious light.³⁹⁶

It is submitted that the New Zealand no asset procedure could be more closely aligned with international principles and guidelines by rendering the moratorium on debt enforcement effective once the application for the procedure is filed. Furthermore, guidelines as regards the means test should be set.³⁹⁷ Comments by academics that the short period attached to the procedure may result in misuse are important and so is the issue that the procedure does not spur the adoption of responsible long-term financial behaviour.³⁹⁸ Although Keeper's suggestion as regards mandatory budgeting or financial literacy courses³⁹⁹ is significant and may prove to be very useful in South Africa, it is doubtful whether such initiatives would be practical in a country with limited resources.

³⁹² 2009.

³⁹³ Ministry of Economic Development *Evaluation of the no asset procedure* 2.

³⁹⁴ See in general Spooner 2013 *ERPL* 747.

³⁹⁵ Ch 2 par 2.7.

³⁹⁶ Brown and Telfer *Personal and corporate insolvency legislation* 37–38 and 41; Telfer 'New Zealand bankruptcy law reform: The new role of the official assignee and the prospects for a no-asset regime' 265–266; Guest 'Introduction: Personal insolvency' 18; Josling 'Introduction' 7; Josling 'Alternatives to bankruptcy' 278 *et seq*; and Keeper 2014 *QUT Law Review* 79.

³⁹⁷ See ch 2 par 2.7.

³⁹⁸ Par 6.5.3. See Telfer 'New Zealand bankruptcy law reform: The new role of the official assignee and the prospects for a no-asset regime' 265–266 and Keeper 2014 *QUT Law Review* 90.

³⁹⁹ Keeper 2014 *QUT Law Review* 90.

In conclusion, it is suggested that South Africa could draw from the New Zealand experience in making a consolidated effort to reform the broader South African debt relief system which will solve problems resulting from the multiple ministries, policies, procedures, forums, regulators and intermediaries involved.

CHAPTER 7: ENGLAND AND WALES DEBT RELIEF

SUMMARY

- 7.1 Introduction
 - 7.2 Historical overview and background
 - 7.3 Bankruptcy
 - 7.4 Alternatives to bankruptcy: Statutory procedures
 - 7.5 Informal procedures
 - 7.6 Conclusion
-

7.1 Introduction

The natural person insolvency system in England and Wales provides for bankruptcy¹ and three formal statutory alternative debt relief procedures in the form of individual voluntary arrangements,² the debt relief order³ and the county court administration order.⁴ Apart from the CCAO procedure, the Insolvency Act⁵ regulates the majority of the jurisdiction's statutory natural person insolvency law. In contrast with the South African position⁶ the system does not discriminate on financial grounds and offers a specific procedure for the so-called No Income No Assets (NINA) debtors⁷ by means of the DRO procedure. This measure became effective on

¹ See pt 9 of the second group of parts of the Insolvency Act 1986 (hereafter 'the Act' or 'the Insolvency Act').

² Hereafter 'IVA'. See pt 8 of the second group of parts of the Insolvency Act.

³ Hereafter 'DRO'. See pt 7A of the second group of parts of the Insolvency Act.

⁴ Hereafter 'CCAO'. See ss 112–117 of the County Court Administration Act 1984. This procedure is not regularly used in practice anymore; Spooner *Personal insolvency law* 90 n655. This research by Spooner is unpublished and cited with the author's permission. See also Spooner 2013 *ERPL* 756 n53.

⁵ Both individual and corporate insolvency are regulated in the Insolvency Act. In South Africa corporate and natural person insolvency are not regulated in one unified Act, although the proposed Insolvency Act contemplates such a combination; see ch 1 par 1.1.

⁶ See ch 1 par 1.1, ch 3 par 3.5 and ch 4 par 4.4 as regards the South African position in this respect.

⁷ It is submitted this this group represents the majority of over-indebted or insolvent South Africans at present; see ch 1 par 1.1. See also Coetzee and Roestoff 2013 *Int Insolv Rev* 189.

6 April 2009 and was inserted into the Insolvency Act by the Tribunals, Courts and Enforcement Act.⁸

As regards the broader system with its various procedures Fletcher submits that⁹

it must be emphasised that bankruptcy itself, in the proper and technical sense of that term, is neither the inevitable nor indeed the appropriate fate of every individual who is approaching, or who has entered, a state of financial insolvency. Provided that the debtor's position is not already irretrievable, the feasibility of a recourse to some form of solution which falls short of a bankruptcy adjudication should preferably be explored. Of these, the one to be chosen will be largely dependent upon the elements of a particular case, and may be either formal or informal in character.

The English system acknowledges that bankruptcy is an 'ultimate' remedy resulting in 'sweeping and profound consequences' for the debtor and his estate and that these very consequences should serve (and are intended to serve) as powerful incentives for those who take up credit to act 'responsibly and honestly towards their creditors'.¹⁰ However, unlike the South African natural person debt relief system,¹¹ the English system's philosophical foundations also include benevolent purposes. These are based on the proposition that the interests of the debtor and society at large are best served in the long run by a legal procedure that aims to provide debt relief where there is no realistic prospect of repaying debt and to thereby offer hope for the future in the form of a rehabilitation and fresh start following a discharge from bankruptcy.¹² The system also provides for different insolvency situations by offering diverse procedures¹³ most of which result in a discharge of honest but unfortunate debtors' debt.¹⁴ In this regard the choice of procedure is mostly dependent on the debtor and not on a court or administrative body.¹⁵ However, the many, sometimes

⁸ 2007. See s 108(1) and sch 17.

⁹ Fletcher *The law of insolvency* 44–45.

¹⁰ *Idem* 43.

¹¹ The South African sequestration procedure is founded on the unilateral concept of advantage for creditors; ch 3 par 3.3.2.2.

¹² Fletcher *The law of insolvency* 43.

¹³ Ramsay 2012 *J Consum Policy* 430.

¹⁴ See the unfair and unreasonable discrimination resulting from mostly the advantage for creditors requirement in the South African system in ch 1 par 1.1, ch 3 par 3.5 and ch 4 par 4.4.

¹⁵ Subject to strict access conditions as regards the DRO procedure; Spooner *Personal insolvency law* 90. See also Spooner 2013 *ERPL* 756. International guidelines are not in agreement as to whether the choice of accessing a particular procedure should be left to the debtor or a disinterested third party. However, the most contemporary report, that of the World Bank, clearly prefers that the decision should be left in the hands of public agencies; *WB Report* 67.

overlapping alternative procedures call for impartial advice by intermediaries as regards the most appropriate measure. In this regard a ‘mixed system’ of public and private debt advice and management has developed, although ‘there remains a substantial public service role in processing consumer bankruptcies through the Official Receiver’.¹⁶

Although the South Africa insolvency system was greatly influenced by English law,¹⁷ it remained stagnant while the system in England and Wales has evolved in response to modern needs. It is due to its progressiveness, the various different procedures that it provides, the attribute of debtors’ choice and its development from the position where South African insolvency law finds itself at present that the system in England and Wales is considered in this study. This chapter thus investigates the natural person insolvency system in England and Wales by considering its most pertinent debt relief procedures both individually and collectively. The investigation, amongst others, measures the system against international principles and guidelines.¹⁸ It also draws comparisons with the South African situation.¹⁹ The ultimate aim is to consider whether any of the system’s attributes could be considered for law reform in South Africa.²⁰

Paragraph two sets out the historic development of and background to the insolvency system for natural persons in England and Wales. The discussion is intended to offer a basic understanding of the system’s progression to its contemporary form. Paragraph three is concerned with the bankruptcy procedure. Alternative statutory measures to bankruptcy, namely the IVA, DRO and CCAO procedures, are discussed in paragraph four. Informal procedures are briefly touched upon in paragraph five for the sake of completeness. The chapter is concluded in paragraph six where the jurisdiction’s features that might be considered as

¹⁶ Ramsay 2012 *J Consum Policy* 430. The official receiver forms part of the UK public service since 1883; *ibid.* It is employed by the insolvency service which is an executive agency of the Department of Trade and Industry; McKenzie Skene and Walters 2006 *Am Bankr LJ* 481.

¹⁷ Roestoff *’n Kritiese evaluasie* 8; Evans *A critical analysis* 13; Steyn *Statutory regulation* 451 and Maghembe *A proposed discharge* 114–115.

¹⁸ See ch 2 in general and specifically par 2.7.

¹⁹ See chs 3 and 4.

²⁰ In this regard Evans notes that the English policy-driven reform ‘can be of considerable value in an attempt to reform South African law’; Evans *A critical analysis* 13.

touchstones when contemplating possible suggestions for South African law reform are highlighted.

7.2 Historical overview²¹ and background

Spooner notes that consumers gained access to natural person insolvency procedures in England and Wales in 1861 when the distinction between traders and non-traders was abolished²² although the first statute dealing with the bankruptcy of natural persons can be traced back to Statute 1542.²³ As is the case of the South African insolvency law, the law in England and Wales was also founded on Roman law – although it was derived from Italian law whereas South African law developed from Roman-Dutch law. Nevertheless, the *cessio bonorum*, *distractio bonorum*, *remissio* and *dilatatio* were present in the early law of England and Wales.²⁴ The law was initially penal in nature and did not distinguish between honest and dishonest debtors.²⁵ Fletcher notes that the law of natural person insolvency ‘attained a state of development which is still recognisable today’ by means of the Bankruptcy Act 1883.²⁶ However, in 1977 the Cork committee was established to conduct the first comprehensive review of the law of insolvency.²⁷ The *Cork Report*, amongst others, suggested a range of procedures to deal with differing insolvency situations.²⁸ Unfortunately the report did not receive the immediate attention that it deserved and only later, during a wave of financial scandals, did some of its proposals gain interest.²⁹ The law has consequently been modernised by the Insolvency Acts of 1985 and 1986, although these laws did not introduce all of the needed recommendations and have in some instances effected drastic changes to the original suggestions.³⁰ The Enterprise Act of 2002 further liberalised the law with the contemporary system being described as a ‘debtors’ paradise’ and as enshrining the

²¹ For an in depth discussion of the history of natural person insolvency law in England and Wales see Fletcher *The law of insolvency*. See also Roestoff ‘*n Kritiese evaluasie 74 et seq* for developments up to 2002.

²² Spooner 2013 *ERPL* 756.

²³ Fletcher *The law of insolvency* 7–9 and n11.

²⁴ *Idem* 8. See ch 3 par 3.2 as regards the origins and history of South African natural person insolvency law.

²⁵ Fletcher *The law of insolvency* 10–11.

²⁶ *Idem* 11.

²⁷ *Idem* 15. See ch 2 par 2.3 for a discussion of the *Cork Report*.

²⁸ See chs 6, 7, 9, 11, 12 and 13.

²⁹ Fletcher *The law of insolvency* 19.

³⁰ *Idem* 20–22.

modern ‘fresh start’ philosophy.³¹ As regards the fresh start, the automatic discharge was first introduced by the Insolvency Act 1976 which provided for a discharge after a period of five years has lapsed since the commencement of bankruptcy proceedings.³² The period was reduced to three years by the Insolvency Act 1986 where after the Enterprise Act further opened the system by reducing the period to twelve months.³³ The latter reform was influenced by the United States of America’s ‘fresh start’ idea.³⁴ However, Ramsay refers to the belief that Europe rather subscribes to an ‘earned start’ and comments that the reform was ‘designed to stimulate entrepreneurialism rather than to provide a safety net for consumers’.³⁵ Nevertheless, he notes that consumers may have been the primary beneficiaries thereof.³⁶ With reference to what was then the Tribunals, Courts and Enforcement Bill and which has consequently introduced the DRO procedure he notes that the policy proposals contained in the Bill³⁷

do not favour a relatively unrestricted access to the bankruptcy discharge for consumers, but rather an expansion of access to repayment plans as the main consumer alternative with a low-cost bankruptcy procedure for the poor debtor with no assets and no likelihood of repaying her debts.

7.3 Bankruptcy

7.3.1 General

McKenzie Skene and Walters describe bankruptcy³⁸ as ‘a judicial procedure for the liquidation of assets of individual debtors’ and as a ‘debt relief tool taking the form of a statutory composition designed to balance the interests of debtors and creditors’.³⁹ The regulating process is contained in part 9 of the Act⁴⁰ and further procedural

³¹ Spooner 2012 *Am Bankr LJ* 248 and authorities cited there. See also Walters 2009 *Int Insolv Rev* 12.

³² See ss 7 and 8.

³³ S 279. See Spooner 2012 *Am Bankr LJ* 253.

³⁴ See ch 2 par 2.2 as regards the American fresh start policy.

³⁵ Ramsay 2006 *U III L Rev* 251 and 255. See also McKenzie Skene and Walters 2006 *Am Bankr LJ* 482.

³⁶ Ramsay 2012 *J Consum Policy* 426–427.

³⁷ *Ibid.*

³⁸ Compare sequestration in the South African system; ch 3 par 3.3.

³⁹ McKenzie Skene and Walters 2006 *Am Bankr LJ* 481. The fact that bankruptcy is regarded as a debt relief tool coincides with international principles and guidelines which focus on the financial rehabilitation of insolvent debtors, but differs from the South African sequestration procedure’s object of advantage for creditors; see ch 2 par 2.7 read together with ch 3 par 3.3.2.2.

⁴⁰ Pt 9 of the Act consists of chs A1–5 which in turn consist of ss 263H–335A.

matters are set out in part 6 of the first group of parts of the Insolvency Rules.⁴¹ Bankruptcy may be applied for by a hostile creditor (or creditors) of the debtor or the debtor himself and entails an application to court.⁴² Although both creditors' and debtors' petitions currently involve the courts, the Enterprise and Regulatory Reform Act,⁴³ the provisions of which have already been rendered effective to some extent, will in future reduce debtors' petitions to administrative procedures.⁴⁴ Bankruptcy commences when a court makes the bankruptcy order⁴⁵ and generally ends, as was mentioned, when the debtor receives an automatic discharge at the end of a period of one year from the date of the order.⁴⁶ A bankruptcy order affects the bankrupt in his personal capacity.⁴⁷ The majority of bankruptcies are processed by the public official receiver⁴⁸ attached to the relevant court.⁴⁹ Lawyers do not play a major role in advising consumers and this role is fulfilled by debt counselling agencies such as the citizens advice bureaux.⁵⁰ Walters observes that⁵¹

consumer bankruptcy can be theorised as a service provided by the state the costs of which are largely borne by its users – that is, debtors and creditors. This contrasts with consumer IVA provision,⁵² which ... is much more a private sector concern.

7.3.2 Access requirements and effect thereof

As was mentioned both a creditor (or creditors) of the debtor or the debtor himself may petition for a bankruptcy order.⁵³ As regards access criteria relating to debtors' applications Spooner notes that although the Act does not contain strict entry requirements, debtors face a considerable financial obstacle as a deposit and fees

⁴¹ Insolvency Rules 1986 (hereafter 'rules').

⁴² S 264(1).

⁴³ 2013.

⁴⁴ S 71, sch 18 inserted ss 263H–263O into the Insolvency Act. The effective date still needs to be determined; s 103. The reduction of court involvement is in line with international principles and guidelines; ch 2 par 2.7.

⁴⁵ S 278.

⁴⁶ S 279(1).

⁴⁷ Both the Insolvency Act and other pieces of legislation lay down legal restraints and disqualifications. See in general Fletcher *The law of insolvency* 370–372.

⁴⁸ Ramsay 2006 *U III L Rev* 252 and 271 and Ramsay 2012 *J Consum Policy* 428.

⁴⁹ Walters 2009 *Int Insolv Rev* 16.

⁵⁰ Ramsay 2006 *U III L Rev* 268–269.

⁵¹ Walters 2009 *Int Insolv Rev* 17.

⁵² See par 7.4.1.

⁵³ S 264. The section also provides for a temporary administrator or liquidator or the supervisor of a person bound by a voluntary arrangement proposed by the debtor to petition. See par 7.4.1 as regards IVAs. The South African sequestration procedure also allows for both debtor and creditor applications; ch 3 par 3.3.1.

amounting to approximately £700 are required.⁵⁴ This is because government does not consider bankruptcies as a 'public good' (that should be financed by the state and individuals) and therefore the 'user pay model' applies.⁵⁵ Nonetheless, Spooner acknowledges that the introduction of the DRO procedure⁵⁶ has alleviated the position,⁵⁷ although a modest fee is also applicable to those applications.⁵⁸

Creditor⁵⁹ petitions are the most common⁶⁰ and are dealt with in sections 267 to 271.⁶¹ Section 267(1) provides that a creditor's petition must be in relation to debts owed by the debtor to that creditor or creditors. Furthermore, a creditor's petition may only be presented to the court if at such time⁶² the debt amount to at least the bankruptcy level⁶³ which is presently set at £750;⁶⁴ the debt is for a liquidated sum owed to the petitioning creditor either immediately or at some certain future date and is unsecured;⁶⁵ it appears that the debtor is unable to pay the debt or does not have

⁵⁴ Spooner *Personal insolvency law* 91. See also *Regina v Lord Chancellor* [2000] Q.B. 597 where the court of appeal held that the required court deposit does not infringe on any constitutional right and is not unlawful. See also Ramsay 2006 *U III L Rev* 271; McKenzie Skene and Walters 2006 *Am Bankr LJ* 484 and Spooner 2012 *Am Bankr LJ* 250. International principles and guidelines suggest that costs should not pose an obstacle to access; ch 2 par 2.7. However, access restricting costs may be justified where sufficient alternative debt relief measures exist.

⁵⁵ Ramsay 2012 *J Consum Policy* 430. Government's view differs from the internationally accepted fact, namely, that insolvency procedures do in fact benefit the larger society; ch 2 par 2.7.

⁵⁶ See par 7.4.2.

⁵⁷ Spooner 2012 *Am Bankr LJ* 250.

⁵⁸ Ramsay 2012 *J Consum Policy* 430.

⁵⁹ A creditor in this context is 'a person to whom any of the bankruptcy debt is owed'; s 383(1)(a). Bankruptcy debt is

- (a) Any debt or liability to which he is subject at the commencement of the bankruptcy,
- (b) Any debt or liability to which he may become subject after the commencement of the bankruptcy (including after his discharge from bankruptcy) by reason of any obligation incurred before the commencement of the bankruptcy,
- (c) ...
- (d) Any interest provable as mentioned in section 322(2) in Chapter IV of Part IX.

S 322(2) provides that interest on bankruptcy debt is provable as part of the debt except where it relates to a period after the commencement of bankruptcy.

⁶⁰ Fletcher *The law of insolvency* 102. International principles and guidelines caution that creditor petitions may be misused; ch 2 par 2.7.

⁶¹ See further ch 2 of pt 6 of the rules.

⁶² S 267(2).

⁶³ S 267(2)(a).

⁶⁴ S 267(4).

⁶⁵ S 267(2)(b). However, such debt need not be unsecured if the petition contains a statement that the person with the right to enforce the security is, for the benefit of all creditors, willing to give up his security if a bankruptcy order is made. Also, the debt need not be secured where the petition is made in respect of the unsecured part of the debt and the petition contains a statement of the estimated value of the security for the secured part; s 269(1). The secured and unsecured parts of the latter mentioned instance will be treated as separate debts for purposes of ss 267 and 270; s 269(2).

a reasonable prospect of being able to pay;⁶⁶ and there is no undetermined application to set aside a statutory demand served⁶⁷ in terms of the debt or any of the debts.⁶⁸

A debtor appears to be unable to pay where the debt is payable immediately and either⁶⁹

- (a) the petitioning creditor to whom the debt is owed has served on the debtor a demand (known as “the statutory demand”) in the prescribed form requiring him to pay the debt or to secure or compound for it to the satisfaction of the debtor, at least 3 weeks have elapsed since the demand was served and the demand has been neither complied with nor set aside in accordance with the rules, or
- (b) execution or other process issued in respect of the debt on a judgment or order of any court in favour of the petitioning creditor, or one or more of the petitioning creditors to whom the debt is owed, has been returned unsatisfied in whole or in part.

The statutory demand was introduced on recommendation of the *Cork Report*⁷⁰ with Fletcher noting that it⁷¹

greatly simplifies and clarifies this area of the law of individual insolvency by replacing the numerous, and highly diversified, ‘acts of bankruptcy’⁷² under the former law with a single, relatively uncomplicated procedure under which the initiative rests entirely with the creditor.

A debtor appears to have no reasonable prospect of being able to pay only if the debt is not payable immediately and⁷³

- (a) the petitioning creditor to whom it is owed has served on the debtor a demand (also known as “the statutory demand”) in the prescribed form requiring him to establish to the satisfaction of the creditor that there is a reasonable prospect that the debtor will be able to pay the debt when it falls due,

⁶⁶ S 267(2)(c). The jurisdiction makes use of the liquidity test which is in line with international principles and guidelines; ch 2 par 2.7.

⁶⁷ Under s 268. In addition to s 268, ch 1 of pt 6 of the rules further regulates statutory demands. See also r 6.11. Compare the proposed South African statutory demand included in the 2015 Insolvency Bill; see ch 3 par 3.3.2.1.

⁶⁸ S 267(2)(d).

⁶⁹ S 268(1).

⁷⁰ Ch 10 para 535–538.

⁷¹ Fletcher *The law of insolvency* 134.

⁷² This development is in line with international principles and guidelines which regard acts of bankruptcy as out-dated as the focus should rather be on inability to pay than on ‘wrongful’ acts of the debtor; ch 2 par 2.7.

⁷³ S 268(2).

- (b) at least 3 weeks have elapsed since the demand was served, and
- (c) the demand has been neither complied with nor set aside in accordance with the rules.

In the event that the petition is wholly or partially based on a debt subject to a statutory demand, the petition may be presented before the three-week period has run out if there is a real possibility that the debtor's property or the value of any of his property will significantly diminish during such period and the petition includes a statement to that effect.⁷⁴

Furthermore, before the court may make a bankruptcy order on a creditor's petition it must be satisfied of one of two things.⁷⁵ The first is that the debt in respect of which the petition is presented is either a debt that is payable at the date of the petition or has become payable since and has not been paid, secured or compounded for.⁷⁶ The second possibility is that the debtor has no reasonable prospect of being able to pay the debt (on which the petition is based) when it falls due.⁷⁷ The court may dismiss a creditor's petition if it is satisfied that the debtor is able to pay all his debts or that he has made an offer to secure or compound for a debt in terms of which the petition is presented, that the acceptance of such an offer would have necessitated the dismissal of the petition and that the offer was unreasonably refused.⁷⁸ Rule 6.25(1) provides that a court may make a bankruptcy order if it is satisfied that the statements in the petition are true and that the debt on which the petition is based has not been paid or secured or compounded for. Also relevant to the court's powers regarding a creditor's petition are the provisions of section 266(2)–(3). Here it is provided that a bankruptcy petition may only be withdrawn with permission of the

⁷⁴ S 270. In these circumstances a court shall not make a bankruptcy order before at least three weeks have lapsed from the service of the statutory demand; s 271(2).

⁷⁵ S 271.

⁷⁶ S 271(1)(a).

⁷⁷ S 271(1)(b). In determining what would establish a reasonable prospect that the debtor will be able to pay debt when it becomes due
it is to be assumed that the prospect given by the facts and other matters known to the creditor at the time he entered into the transaction resulting in the debt was a reasonable prospect; s 271(4).

⁷⁸ S 271(3).

court,⁷⁹ which provides an important safeguard against creditor misuse.⁸⁰ Furthermore, the court has a general power to, in appropriate instances (where the rules were infringed or for any other reason), dismiss a bankruptcy petition, stay proceedings in terms of a bankruptcy petition and where the latter order is made, to also set terms and conditions.⁸¹ It is interesting that a court may dismiss a bankruptcy petition where the continuation of the proceedings would result in waste of energy and money due to the lack of assets for distribution amongst creditors.⁸² However, the court will make a bankruptcy order where the bankrupt may acquire property, where bankruptcy expenses would swallow the proceeds of assets⁸³ or where it is probable as opposed to certain that there are no assets.⁸⁴

As regards debtors' petitions, they will not in future involve the courts and will be dealt with by an administrative procedure.⁸⁵ However, at present debtors still need to petition the courts. Nevertheless, the process as set out in sections 272 to 275⁸⁶ is tremendously 'process friendly'.⁸⁷ Debtor petitions may only be based on the grounds that the debtor is unable to pay his debts⁸⁸ which also embody the 'only substantive eligibility requirement'.⁸⁹ The petition must be accompanied by a statement of the debtor's affairs including particulars relating to his creditors, debts, other liabilities and assets.⁹⁰ It must also include other prescribed information.⁹¹ It is notable that debtors are not required to notify creditors in advance and that no obligatory pre-petition procedural 'hurdles' are prescribed.⁹² Although debtors'

⁷⁹ S 266(2). See also r 6.32.

⁸⁰ Fletcher *The law of insolvency* 161. International principles and guidelines warn against the abuse of creditor petitions; ch 2 par 2.7.

⁸¹ S 266(3).

⁸² *Ex parte Robinson in re Robinson* (1883) 22 Ch.D. 816; *In re Otway ex parte Otway* [1895] 1 Q.B. 812 (CA); *In re Emma Somers, ex parte Union Credit Bank Limited* (1897) 4 Mans. 227 as well as the discussion in Fletcher *The law of insolvency* 165 *et seq.* See the South African position where assets are necessary to satisfy the advantage requirement; ch 3 par 3.3.2.2.

⁸³ *Re Jubb* [1897] 1 Q.B. 641 QBD.

⁸⁴ *In re Leonard ex parte Leonard* [1896] 1 Q.B. 473 (CA) and *Re Birkin* (1896) 3 Mans. 291. See also Fletcher *The law of insolvency* 165–166.

⁸⁵ S 71, sch 18 of the Enterprise and Regulatory Reform Act inserted ss 263H–263O into the Insolvency Act. The effective date still needs to be determined; s 103. The reduction of court involvement is in line with international principles and guidelines; ch 2 par 2.7.

⁸⁶ See further ch 3 of pt 6 of the rules.

⁸⁷ Walters and Smith 2010 *Int Insolv Rev* 192.

⁸⁸ S 272(1).

⁸⁹ Walters and Smith 2010 *Int Insolv Rev* 191.

⁹⁰ S 272(2)(a). See further s B of ch 5 of pt 6 of the rules. The filing of the petition and the statement of affairs and the payment of the court fee and deposit are the only procedural requirements; Walters and Smith 2010 *Int Insolv Rev* 192.

⁹¹ S 272(2)(b).

⁹² Walters and Smith 2010 *Int Insolv Rev* 192.

petitions were described as relatively ‘straightforward’ as the debtor consents thereto,⁹³ the courts enjoy wide discretion as was mentioned in the context of creditors’ petitions.⁹⁴ However, a court has to first apply the test in section 273(1) before setting out to decide whether to grant a bankruptcy order or not. As will be seen from the discussion below, this test is intended to channel appropriate cases to the IVA procedure.⁹⁵ Section 273(1) provides that, subject to section 274, the court shall not make a bankruptcy order if it appears that if such order is made the aggregate amount of the unsecured bankruptcy debt would be less than the small bankruptcies level which is presently set at £40 000;⁹⁶ that if the order is made, the value of the estate would be equal to or more than the minimum amount which is presently set at £4 000;⁹⁷ that within the preceding five years the debtor has not been adjudicated bankrupt or entered into a composition with his creditors or scheme of arrangement of his affairs;⁹⁸ and that in the court’s estimation it would be appropriate to appoint a person to compile a report in terms of section 274.⁹⁹ Therefore, where these circumstances are present, the court must appoint an insolvency practitioner to prepare a report in terms of section 274 and (subject to section 258(3))¹⁰⁰ to act in relation to a voluntary arrangement to which the report relates.¹⁰¹

A person appointed in terms of section 273 must investigate the debtor’s affairs and in his report, that must be submitted to court, indicate whether the debtor is willing to make a proposal for an IVA,¹⁰² and if so, whether a meeting of creditors should be summoned to consider the proposal as well as the date, time and place of the

⁹³ Fletcher *The law of insolvency* 166.

⁹⁴ S 264(2) and s 266(3). See also Fletcher *The law of insolvency* 167.

⁹⁵ See par 7.4.1. Unlike the South African position, the Act clearly sets out the interplay between the bankruptcy procedure and alternative measures. See also below. As regards the South African position see ch 3 par 3.3.2.3 and ch 4 para 4.2.5 and 4.3.4 which illustrate the difficulties that arise when the legislature does not consider the interplay between procedures.

⁹⁶ S 273(1)(a). See the Insolvency Proceedings (Monetary Limits) Order 1986 (SI 1986/1996) as amended and referred to by Fletcher *The law of insolvency* 167.

⁹⁷ S 273(1)(b). See the Insolvency Proceedings (Monetary Limits) Order 1986 (SI 1986/1996) as amended and referred to by Fletcher *The law of insolvency* 167.

⁹⁸ S 273(1)(c).

⁹⁹ S 273(1)(d).

¹⁰⁰ See par 7.4.1.

¹⁰¹ S 273(2).

¹⁰² S 274(1).

proposed meeting.¹⁰³ The court may then either make an interim order¹⁰⁴ in terms of section 252, for the purpose of facilitating the consideration and implementation of the proposal, or make a bankruptcy order.¹⁰⁵ If the first order is made a meeting shall be summoned which is deemed to have been summoned in terms of section 257 and subsections (2) and (3) of that section and sections 258 to 263 will apply accordingly.¹⁰⁶

Where the court is of the opinion that a DRO would have been made if the debtor had applied therefor in terms of part 7A¹⁰⁷ and that it would be in the best interest of the debtor to so apply the court may refer the debtor to an approved intermediary to set the process in motion.¹⁰⁸ In such instances the court shall stay proceedings in terms of the petition on conditions that it deems fit, but once a DRO is made, the petition shall be dismissed.¹⁰⁹

Section 276 sets out special considerations as regards bankruptcy petitions where the debtor is subject to a voluntary arrangement. It provides that where an IVA order has already been made and a person (other than the debtor) thereafter petitions for the debtor's bankruptcy¹¹⁰ the court shall only make such an order¹¹¹ where the debtor has failed to comply with his obligations in terms of the voluntary arrangement;¹¹² material false or misleading information or omissions were contained in the statement of affairs or other documents supplied in terms of part 8¹¹³ or were otherwise made available to creditors at or in relation to a meeting summoned in terms of the mentioned part;¹¹⁴ or that the debtor has failed to do all

¹⁰³ S 274(2).

¹⁰⁴ The interim order ceases to have effect at the end of a period specified by the court for enabling the consideration of the proposal; s 274(4).

¹⁰⁵ S 274(3).

¹⁰⁶ S 274(5). These sections set out procedural aspects relating to the IVA procedure; see par 7.4.1.

¹⁰⁷ S 274A(1)(a). S 274A should be read together with r 5A.22. See also r 5A.23 as regards a petitioning creditor's consent to the making of an application for a DRO.

¹⁰⁸ S 274A(2).

¹⁰⁹ S 274A(3). See par 7.4.2 as regards the DRO procedure. Once again, the Insolvency Act clearly regulates the interplay between the bankruptcy and alternative procedures which differs from the South African position; see ch 3 par 3.3.2.3 and ch 4 para 4.2.5 and 4.3.4.

¹¹⁰ In terms of s 264(1)(c).

¹¹¹ If a bankruptcy order is made in such circumstances, the expenses incurred in relation to the IVA will be a first charge against the bankrupt's estate; s 276(2).

¹¹² S 276(1)(a).

¹¹³ S 276(1)(b)(i).

¹¹⁴ S 276(1)(b)(ii).

that was reasonably required of him by the supervisor.¹¹⁵ Remarkably, a debtor cannot use this section to apply for a bankruptcy order once he has convinced his creditors to accept a proposal for a voluntary arrangement – which provides an important safeguard against debtors’ potential tactical defaults and consequent bankruptcy petitions.¹¹⁶

As far as individual enforcement and execution proceedings are concerned, the system does not provide for a general automatic moratorium once an application is filed. This is as section 285 provides that where proceedings in terms of a bankruptcy petition are pending or where a debtor has been adjudged bankrupt¹¹⁷

the court *may* stay any action, execution or other legal process against the property or person of the debtor or, as the case may be, of the bankrupt.

However, once a bankruptcy order has been made, creditors, except for secured creditors,¹¹⁸ who are owed a debt provable in bankruptcy do not have a remedy against the property or person of the bankrupt (regarding such debt) and may not prior to the bankrupt’s discharge commence any action or other legal processes (against the bankrupt) except with permission of the court and on terms that it may impose.¹¹⁹ As for others, the court in which individual proceedings are pending may stay such proceedings or allow them to continue on terms that it deems fit.¹²⁰

A last consideration is that, where necessary to protect the debtor’s property, the court may appoint the official receiver as an interim receiver (of the debtor’s property) between the presentation of a bankruptcy petition and the moment when the actual bankruptcy order is made.¹²¹

¹¹⁵ S 276(1)(c). Where the bankruptcy order is made, the court may, if it deems it appropriate, appoint the supervisor of the IVA as trustee of the estate; s 297(5). Once again, it is clear from the above discussions that the interplay between the different statutory proceedings is well thought through, unlike the position in South Africa where the failure to do so has resulted in unintended and undesirable consequences; see ch 3 par 3.3.2.3 and ch 4 par 4.3.4.

¹¹⁶ Fletcher *The law of insolvency* 150.

¹¹⁷ S 285(1). My emphasis.

¹¹⁸ S 285(4). The protection of secured creditors’ rights are in line with international principles and guidelines; ch 2 par 2.7.

¹¹⁹ S 285(3). However, international guidelines favour the position where a moratorium on debt enforcement becomes effective once an application is lodged; ch 2 par 2.7.

¹²⁰ S 285(2).

¹²¹ S 286(1). See further s 286(2)–(8). See also ch 4 of pt 6 of the rules.

7.3.3 General process following a bankruptcy order

Once a bankruptcy order has been made, whether as a consequence of a debtor's petition or that of a creditor(s), the same general procedure follows.¹²² The official receiver becomes the receiver and manager of the estate property¹²³ which he must protect¹²⁴ in the interest of the creditors. The bankrupt must deliver possession of his estate and relevant documents to the official receiver.¹²⁵ The official receiver will later, in appropriate circumstances, be substituted by a duly elected trustee¹²⁶ and the bankrupt must cooperate with both the official receiver and the trustee.¹²⁷ The trustee is usually elected by creditors from the ranks of private insolvency practitioners¹²⁸ who are mostly accountants.¹²⁹ In practice, private sector trustees are only appointed where the estate holds sufficient assets to render such an appointment worthwhile or where some issues are in need of a full investigation and possible challenge in terms of avoiding powers.¹³⁰ If no such appointment is made, the official receiver will become the trustee.¹³¹

Before the substitution of the official receiver for the trustee takes place, the official receiver has to carry out a number of statutory duties. These duties include an initial investigation into the bankrupt's conduct and affairs¹³² to determine the reasons for his insolvency and to establish the value and whereabouts of assets of the estate as well as the validity and amount of alleged liabilities. In this regard an application may be lodged to the court to summon the bankrupt and other persons of interest to appear before it as part of an inquiry into the bankrupt's dealings and property.¹³³ To assist the official receiver in his duties the bankrupt must prepare a statement of his affairs,¹³⁴ although this will only be necessary where the bankruptcy order is made in

¹²² See rr 6.33–6.35 as regards creditors' petitions and rr 6.45–6.47 relating to debtors' petitions. These rules are similarly worded; see Fletcher *The law of insolvency* 171 n 1.

¹²³ S 387(1).

¹²⁴ S 387(2).

¹²⁵ S 291(1).

¹²⁶ S 292. See also in general ch 10 of pt 6 of the rules as regards the trustee in bankruptcy.

¹²⁷ Ss 291 and 333.

¹²⁸ See s 292(1)(a) and (b).

¹²⁹ McKenzie Skene and Walters 2006 *Am Bankr LJ* 481.

¹³⁰ *Ibid.*

¹³¹ See for instance ss 293(3) and 295(4).

¹³² S 389(1)(a).

¹³³ S 366(1).

¹³⁴ S 288(1). See further s A of ch 5 of pt 6 of the rules.

terms of a creditor's petition.¹³⁵ The official receiver will eventually report his findings to the court¹³⁶ and such report becomes part of the bankruptcy record which may be used in several instances, such as determining the desirability of a public examination in court¹³⁷ and when the bankrupt's discharge is under consideration.¹³⁸ Nevertheless, the official receiver need not conduct an investigation and make a report where he is of the opinion that such an investigation is unnecessary.¹³⁹ Another important duty of the official receiver is to determine whether there are sufficient assets to justify a creditors' meeting¹⁴⁰ to appoint a trustee.¹⁴¹ In the event that the official receiver decides not to summon such a meeting, he must forward a notice to the court and creditors where after he becomes the trustee.¹⁴²

If and when a trustee is appointed,¹⁴³ the estate vests in him¹⁴⁴ and where no trustee is appointed, the official receiver fulfils the role.¹⁴⁵ According to section 306(2) the vesting takes place automatically as

[w]here any property which is, or is to be, comprised in the bankrupt's estate vests in the trustee ... it shall so vest without any conveyance, assignment or transfer.

Section 436 affords a very wide meaning to property as including

money, goods, things in action, land and every description of property wherever situated and also obligations and every description of interest whether present or future or vested or contingent, arising out of, or incidental to, property.

¹³⁵ *Ibid.*

¹³⁶ S 289(1)(b).

¹³⁷ S 290. See also ch 13 of pt 6 of the rules as regards the public examination of the bankrupt.

¹³⁸ S 289(3) read together with s 280.

¹³⁹ S 289(2). See Department of Trade and Industry *Insolvency – A second chance* para 1.40 and 1.41.

¹⁴⁰ See ch 7 of pt 6 of the rules as regards creditors' meetings. To only conduct a creditors' meeting where the estate represents sufficient assets is in line with international principles that favour the exclusion of creditor participation as a matter of course – except where the estate represents significant value; ch 2 par 2.7.

¹⁴¹ S 293. Where the meeting fails to appoint a trustee, the official receiver must decide whether to refer the matter to the secretary of state for appointment or not. If the matter is not referred to the secretary or where it declines to make an appointment, the official receiver becomes the trustee in the estate; s 295.

¹⁴² S 293(2) and (3). However, the official receiver must summon a meeting when requested to do so by one quarter in value of creditors; s 294(1) and (2).

¹⁴³ See in general pt 9 ch 3 as regards the trustee in bankruptcy.

¹⁴⁴ S 306(1).

¹⁴⁵ *Ibid.*

The trustee is generally controlled by the court¹⁴⁶ and also by the creditors' committee or in certain instances by the secretary of state.¹⁴⁷ The trustee must administer the estate¹⁴⁸ with section 305(2) detailing his general functions in the following terms:

to get in, realise and distribute the bankrupt's estate in accordance with the following provisions of this Chapter; and in the carrying out of that function and in the management of the bankrupt's estate the trustee is entitled, subject to those provisions, to use his own discretion.

Section 283 provides that a bankrupt's estate comprises of property belonging to or which is vested in the bankrupt at the time when the bankruptcy takes effect.¹⁴⁹ It also includes property that the Act specifically specifies as such.¹⁵⁰ However, the following property is specifically excluded from the estate¹⁵¹

- (a) such tools, books, vehicles¹⁵² and other items of equipment as are necessary to the bankrupt for use personally by him in his employment, business or vocation;
- (b) such clothing, bedding, furniture, household equipment and provisions as are necessary for satisfying the basic domestic needs of the bankrupt and his family.

Although no monetary limit is set on the above categories of exempt items, such property may be reclaimed by the trustee where they represent 'excess value'.¹⁵³ A 'reclaim' will be appropriate where it appears to the trustee that the realisable value of the property is more than the cost of reasonable replacement thereof.¹⁵⁴ Where such property is reclaimed, the trustee must apply estate funds to replace such property.¹⁵⁵ Evans also mentions other property that is excluded from the bankrupt

¹⁴⁶ S 303.

¹⁴⁷ Ss 301 and 302. See also s 304 as regards the liability of the trustee.

¹⁴⁸ See in general pt 9 ch 4.

¹⁴⁹ S 283(1)(a).

¹⁵⁰ S 283(1)(b).

¹⁵¹ S 283(2). Compare the South African system regarding excluded and exempted property; ch 3 par 3.3.3.

¹⁵² A vehicle exemption is foreign to South African insolvency law; see ch 3 par 3.3.3.

¹⁵³ S 308. International principles and guidelines propose a standards-based approach where most property is exempted and where the obligation to claim assets of excess value is placed on the insolvency representative; ch 2 par 2.7. England and Wales partly adhere to these benchmarks and stand in stark contrast with the unsatisfactory South African position as regards exempt property; see ch 3 par 3.3.3.

¹⁵⁴ S 308(1).

¹⁵⁵ S 308(3). See further ch 15 of pt 6 of the rules.

estate on the basis of statutory provisions, case law and specific arrangements between the debtor and other persons.¹⁵⁶ These are

- a. awards for personal damages;¹⁵⁷
- b. trust property;¹⁵⁸
- c. legacies which are forfeited on strength of a will in insolvent circumstances, or where a discretionary trust is created and where the trustees must decide whether a beneficiary may benefit from the will;¹⁵⁹ and
- d. rights to pension.¹⁶⁰

Not only property forming part of the estate at the commencement of bankruptcy, but also property that the bankrupt has acquired or which has devolved upon him thereafter may be claimed by the trustee.¹⁶¹ Where, after the commencement of the bankruptcy, property is acquired by or devolves upon the bankrupt or where there is an increase in his income, he must notify the trustee,¹⁶² who then has 42 days to serve a notice on the debtor claiming the after-acquired property.¹⁶³ Regarding income specifically and in line with the 'can pay should pay' principle¹⁶⁴ section 310 provides that the trustee may apply to court for an income payment order at any time before the bankrupt is discharged.¹⁶⁵ However, the court shall not make an order having the effect of reducing the bankrupt's income to below what is necessary to meet his and his family's reasonable domestic needs.¹⁶⁶ The effect of such an order may continue after the bankrupt is discharged, but may not end more than three years from the date on which the order is made.¹⁶⁷ The bankrupt and his trustee or

¹⁵⁶ Evans *A critical analysis* 122–130.

¹⁵⁷ See also Fletcher *The law of insolvency* 227 and authorities cited there.

¹⁵⁸ S 283(3)(a). See also Fletcher *The law of insolvency* 250–252.

¹⁵⁹ See also Fletcher *The law of insolvency* 255 *et seq* and authorities cited there.

¹⁶⁰ *Idem* 262–265. See also s 342A, B and C.

¹⁶¹ S 307(1). See Evans *A critical analysis* 118–122 and Fletcher *The law of insolvency* 238 *et seq*.

¹⁶² S 333(2) read together with r 6.200.

¹⁶³ S 309(1)(a). See also ch 19 of pt 6 of the rules as regards after-acquired property.

¹⁶⁴ Department of Trade and Industry *Insolvency – A second chance* par 1.20.

¹⁶⁵ S 310(1) and (1A). See further ch 16 of pt 6 of the rules. See also Fletcher *The law of insolvency* 242–245. The income payment order feature is in line with international principles as the debtor should do the best that he can to be rewarded with the discharge at the end of the term; ch 2 par 2.7.

¹⁶⁶ S 310(2). Fletcher submits that a determination of reasonable domestic needs 'will be a question of fact in each case'; Fletcher *The law of insolvency* 244. This is contrary to international guidelines that prefer a standards-based approach supplemented by an element of discretion; ch 2 par 2.7.

¹⁶⁷ S 310(6).

the official receiver may also conclude an income payments agreement which has a similar effect than an income payments order.¹⁶⁸ Fletcher mentions that the main advantage of an agreement as opposed to an order is savings in costs, especially those relating to an application to court.¹⁶⁹

While not a specific focus of this thesis, special mention has to be made of the position relating to the bankrupt's home.¹⁷⁰ Although insolvency law did not conventionally recognise a homestead exemption, section 313A was inserted into the Insolvency Act by section 261(3) of the Enterprise Act which now provides for a 'low equity' home exemption.¹⁷¹ The trustee must further obtain a court order before he may sell the bankrupt's home.¹⁷² In appropriate circumstances, the bankruptcy court is also allowed to delay the sale thereof.¹⁷³

Evans states that the system 'appears to have achieved an acceptable balance between all stakeholders' and that '[a]t worst, the bankrupt and his dependants retain a considerable estate and, where relevant, a home'.¹⁷⁴ He explains that the Act provides for the automatic vesting of the estate in the trustee which estate in essence includes all property at the commencement of the bankruptcy and a potentially substantial part of after-acquired property but that generous provision is also made for exempt property. As regards after-acquired property, the trustee on the one hand has extensive powers to claim such property, but must do so within a limited period of time. On the other hand, the bankrupt may possibly retain a

¹⁶⁸ S 310A. See further ch 16A of pt 6 of the rules. See also Fletcher *The law of insolvency* 245–246.

¹⁶⁹ Fletcher *The law of insolvency* 246.

¹⁷⁰ For a thorough and detailed exposition of the position of the bankrupt's home in England and Wales see Steyn *Statutory regulation* 467–491. See also the various legislative directions stemming from several pieces of legislation that may impact on relevant rights as discussed by the author. See further Evans *A critical analysis* 113–118; Fletcher *The law of insolvency* 232 *et seq* and Steyn 2013 *Int Insolv Rev* 154 *et seq*.

¹⁷¹ See Steyn 2012 *De Jure* 640.

¹⁷² S 337.

¹⁷³ See ss 336 and 337. See also ss 335A, 313, 313A and 283A. International principles and guidelines are hesitant to suggest a homestead exemption in insolvency law, but encourage jurisdictions to consider interests in relation thereto; see WB *Report* 79 specifically and further 105–114.

¹⁷⁴ Evans *A critical analysis* 133.

substantial part of his after-acquired assets which contribute to his new estate and a fresh start.¹⁷⁵

7.3.4 Discharge and annulment and their effects

Section 278 provides that bankruptcy commences once the order has been made and continues until the individual is discharged in terms of ‘the following provisions of this chapter’. Sections 279 to 282 then describe the termination of bankruptcy upon a discharge or annulment.¹⁷⁶

As was mentioned,¹⁷⁷ section 279 provides that an automatic discharge¹⁷⁸ takes place once a period of one year has lapsed since the bankruptcy order was made.¹⁷⁹ Before the Enterprise Act substituted the content of the section to reflect its present status¹⁸⁰ it provided for a discharge after a period of three years. Fletcher mentions that the shorter period after which an automatic discharge takes place has been balanced by provisions (which are discussed below) providing for a court suspension of the procedure and new powers as regards post-discharge restrictions where the bankrupt’s ‘conduct is deemed to have been socially unsatisfactory’.¹⁸¹ McKenzie Skene and Walters also comment that the Enterprise Act’s loosening of the discharge policy was not intended to transform bankruptcy into a ‘soft touch’.¹⁸² Section 279(2) provided that a bankrupt may be discharged earlier than the one-year period in instances where the official receiver concluded that the bankruptcy was due to misfortune and that the debtor was *bona fide*. However, this provision was repealed by the Enterprise and Regulatory Reform Act.¹⁸³ Furthermore, although section 280 provides for a discharge by order of court it is (due to, amongst others,

¹⁷⁵ *Idem* 132–133.

¹⁷⁶ See Fletcher *The law of insolvency* ch 11 as regards the termination of bankruptcy by discharge or annulment.

¹⁷⁷ Par 7.3.1.

¹⁷⁸ The automatic discharge was first introduced in 1976; Fletcher *The law of insolvency* 363.

¹⁷⁹ S 279(1). This is contrary to the South African position where an automatic discharge only takes place after ten years; ch 3 par 3.3.4.

¹⁸⁰ See s 256(1).

¹⁸¹ Fletcher *The law of insolvency* 362. See ss 279(3) and 281A. The suspension of a discharge only occurs in an extremely low percentage of cases; Spooner 2012 *Am Bankr LJ* 253.

¹⁸² McKenzie Skene and Walters 2006 *Am Bankr LJ* 282.

¹⁸³ S 73, sch 21, pt 3 par 5.

the reforms as regards the discharge period) not actively pursued in practice any more.¹⁸⁴

Regarding the suspension of the procedure, section 279(3) and (4) provides that where the bankrupt fails to comply with an obligation in terms of part 9, the official receiver or trustee may apply to court for an order suspending the running of the one-year period after which an automatic rehabilitation becomes effective. If the court is satisfied that the bankrupt failed to or is failing to comply with an obligation, it may order that the period will cease to run until a specified date or until a specified condition¹⁸⁵ has been fulfilled.¹⁸⁶

The Enterprise Act¹⁸⁷ inserted section 281A into the Insolvency Act, rendering schedule 4A of effect. The schedule relates to bankruptcy restriction orders¹⁸⁸ and undertakings¹⁸⁹ which substituted previous stigmatising restrictions, prohibitions and disqualifications that applied automatically to all bankrupts.¹⁹⁰ The reason behind the reform was that the public and business community need to be protected against only a small minority of irresponsible, reckless or otherwise culpable bankrupts.¹⁹¹ It appears that this rationale is secure as statistics show that the percentage of bankruptcies resulting in bankruptcy restriction orders and undertakings is small.¹⁹² The basic difference between restrictions and undertakings is that bankruptcy

¹⁸⁴ Fletcher *The law of insolvency* 346.

¹⁸⁵ This includes a condition that the court be satisfied of something; s 279(5).

¹⁸⁶ S 279(3)–(4). S 279 does not affect the power of the court to annul a bankruptcy order; s 279(7). See the discussion of annulment below. See also rr 6.215 and 6.176(4). International principles and guidelines provide that good behaviour may be set as a condition for the discharge and creditors and state agencies may play a role in challenging same – yet criteria for challenges should be clear; ch 2 par 2.7. It is submitted that the system adheres to these guidelines.

¹⁸⁷ S 257(1) and (2), sch 20.

¹⁸⁸ Para 1–6 of the schedule. See also ch 28 of pt 6 of the rules. See further Department of Trade and Industry *Insolvency – A second chance* para 1.25–1.39.

¹⁸⁹ Department of Trade and Industry *Insolvency – A second chance* para 7–9. See also ch 30 of pt 6 of the rules.

¹⁹⁰ Department of Trade and Industry *Insolvency – A second chance* para 1.4, 1.6, 1.21–1.24. See also McKenzie Skene and Walters 2006 *Am Bankr LJ* 482–483, Walters 2009 *Int Insolv Rev* 12 and Spooner 2013 *ERPL* 758. The removal of obsolete and damaging restrictions, disqualifications and prohibitions coincides with international principles and guidelines; ch 2 par 2.7.

¹⁹¹ Department of Trade and Industry *Insolvency – A second chance* executive summary and par 1.3.

¹⁹² Spooner 2012 *Am Bankr LJ* 255.

restriction orders are effected by the court¹⁹³ whereas bankruptcy restriction undertakings involve an undertaking by the bankrupt to the secretary of state which then accepts it as such.¹⁹⁴ A bankruptcy restriction order may only be applied for by the secretary of state or an official receiver acting on its direction¹⁹⁵ and the application must generally be made within a period of one year¹⁹⁶ from the date on which the bankruptcy commences.¹⁹⁷ Where the period has expired, the permission of the court is necessary to make an application of this kind.¹⁹⁸ The court shall grant such order if it deems it appropriate having regard to the bankrupt's conduct whether before or after the bankruptcy order was made.¹⁹⁹ Paragraph 2(2) sets out kinds of behaviour that the court shall in particular take into account. These, for instance, relate to the failure to produce records as were demanded by the official receiver or trustee, giving preference, making excessive pension contributions, fraud or fraudulent breach of trust and failure to cooperate with the official receiver or the trustee. Furthermore, the court must in particular consider whether the bankrupt is a 'repeat bankrupt' in that he was an undischarged bankrupt during the six years preceding the bankruptcy to which the application relates.²⁰⁰ Fletcher notes that this consideration constitutes 'a necessary counterbalance to the more liberal policy towards the granting of automatic discharge after one year'.²⁰¹ The order becomes effective when it is made and shall continue to be effective until the date specified therein.²⁰² However, such date must be at least two years from the date on which the order is made but not more than fifteen years therefrom.²⁰³ The court may make an interim bankruptcy restriction order where it is of the opinion that *prima facie* grounds for a successful application for a bankruptcy restriction order exist and where it would be in the public interest to make such an order.²⁰⁴ This will essentially be

¹⁹³ See par 1(1).

¹⁹⁴ Fletcher *The law of insolvency* 372.

¹⁹⁵ Par 1.

¹⁹⁶ However, this period ceases to run where the period set for discharge is suspended in terms of s 279(3). See above.

¹⁹⁷ Par 3(1)(a). This period coincides with the period after which an automatic discharge becomes effective; s 279(1).

¹⁹⁸ Par 3(1)(b).

¹⁹⁹ Par 2(1).

²⁰⁰ Par 2(3).

²⁰¹ Fletcher *The law of insolvency* 374.

²⁰² Par 4(1).

²⁰³ Par 4(2).

²⁰⁴ Par 5(2). See also para 5 and 6 as regards interim orders in general. See further ch 29 of pt 6 of the rules.

where the bankrupt would be discharged before the hearing of the bankruptcy restriction application is completed which would render the public vulnerable to potentially damaging conduct by the bankrupt in the meantime.²⁰⁵ As was mentioned, bankruptcy restriction undertakings are in essence akin to bankruptcy restriction orders save for the fact that the bankrupt offers such undertaking to the secretary of state who must decide whether to accept it or not – having regard to the matters set out in paragraph 2(2) and (3).²⁰⁶

It is important to note that bankruptcy restriction orders and undertakings do not affect the discharge, but limits the debtor's ability to re-enter the 'credit economy'. This is as post-discharge restrictions, for instance to act in various capacities such as a company director or an insolvency practitioner, and to obtain credit above a prescribed amount, are imposed on the debtor. These restrictions²⁰⁷

[a]re a matter of public record that, in theory, should improve the information available to credit markets and affect credit scoring by enabling lenders to differentiate between culpable and non-culpable debtors.

The most significant effect of a discharge is that it releases the bankrupt from all bankruptcy debts.²⁰⁸ However, the right of secured creditors to enforce their securities remains.²⁰⁹ Furthermore, the bankrupt is not released from debts which he incurred in relation to fraud or fraudulent breach of trust to which he was a party;²¹⁰ relating to a fine for an offence and liability under a recognisance;²¹¹ in the form of damages for personal injuries to another resulting from negligence, nuisance or breach of statutory, contractual or other duty or to pay damages in terms of part 1 of the Consumer Protection Act²¹² and debts that arose in terms of an order made in family proceedings relating to the Child Support Act²¹³ – except to the extent and on

²⁰⁵ Fletcher *The law of insolvency* 375. See also *Official Receiver v Merchant* [2006] B.P.I.R. 1525 Ch.D. where it was held that the court must be satisfied of sufficient reasons for making such an interim order.

²⁰⁶ Par 7.

²⁰⁷ McKenzie Skene and Walters 2006 *Am Bankr LJ* 483. See also Walters 2009 *Int Insolv Rev* 13.

²⁰⁸ S 281(1).

²⁰⁹ S 281(2). This is in line with international principles and guidelines; ch 2 par 2.7.

²¹⁰ S 281(3). It also relates to instances where forbearance in relation to debt was secured in the same manner.

²¹¹ S 281(4). However, treasury may consent to a release where the liability relates to public revenue or a recognisance connected thereto.

²¹² 1987.

²¹³ 1991.

conditions that the court may direct,²¹⁴ and that are not provable in bankruptcy.²¹⁵ The discharge relates to the liability of the bankrupt only and not to others who may be liable for the same debts.²¹⁶ It is important to note that a creditor's right of recourse against a discharged bankrupt and for debts that were discharged will not revive where the debtor merely promises to pay.²¹⁷ However, it may revive where 'fresh consideration is furnished by the creditor in return for the discharged bankrupt's promise to pay'.²¹⁸ Nevertheless, the discharge is generous as bankruptcy debts are broadly defined and non-dischargeable debts are restricted.²¹⁹

The discharge generally lifts all legal restraints and disqualifications relating to the bankrupt.²²⁰ However, the bankrupt's position is not completely restored. This is so since an income payments order²²¹ may extend beyond the time when the discharge becomes effective, although it does not hinder the discharge itself,²²² and bankruptcy restriction orders may continue for up to fifteen years.²²³ A bankrupt must further continue to assist the trustee to fulfil his functions²²⁴ and inquiries into the bankrupt's dealings and property may also continue.²²⁵

To draw the discussion on the discharge feature to a close, comments by pertinent authors regarding reforms are appropriate. McKenzie Skene and Walters observe that the extent to which the Enterprise Act liberalised bankruptcy is contested²²⁶ as it may be argued that the combination of income capture and post-discharge restrictions as well as the public nature of the process render it a tough option.

²¹⁴ S 281(5).

²¹⁵ S 281(6). See r 6.223 which provides that obligations relating to a confiscation order made in terms of s 1 of the Drug Trafficking Offences Act 1986, s 1 of the Criminal Justice (Scotland) Act 1987, or s 71 of the Criminal Justice Act 1988 or pts 2, 3 or 4 of the Proceeds of Crime Act 2002 are not released. See further Fletcher *The law of insolvency* 367 *et seq.*

²¹⁶ S 281(7).

²¹⁷ *Heather and Son v Webb* (1876) L.R. 2 C.P.D. 3.

²¹⁸ See Fletcher *The law of insolvency* 368.

²¹⁹ McKenzie Skene and Walters 2006 *Am Bankr LJ* 482. See also Walters and Smith 2010 *Int Insolv Rev* 191. The generous discharge is in line with international principles and guidelines; ch 2 par 2.7.

²²⁰ See Fletcher *The law of insolvency* 370–372. This is in line with international principles and guidelines; ch 2 par 2.7.

²²¹ See s 310. See par 7.3.3.

²²² See Walters and Smith 2010 *Int Insolv Rev* 191 n45.

²²³ See above.

²²⁴ S 333(3).

²²⁵ S 366. See in general Fletcher *The law of insolvency* 369–370.

²²⁶ McKenzie Skene and Walters 2006 *Am Bankr LJ* 483.

However, others suggest that it has become an ‘easy ride’ to a fast and wide discharge as opposed to alternative procedures.²²⁷ Furthermore as regards the changing law relating to the discharge and its wider consequences Fletcher makes the following observations which are indispensable in a comparative study:²²⁸

The removal in 1976 of the former requirement for all bankrupts to make personal application to the court in order to obtain their discharge, and the substitution of the concept of a fixed, and progressively shortened, duration of the condition of bankruptcy for those debtors who respect their legal obligations while they remain undischarged, undoubtedly marked the beginning of a fundamental adjustment in prevailing social attitudes towards bankruptcy, and towards those who undergo it. For the so-called ‘deserving’ debtor, at any rate, the aura of menace and near-perpetual stigma which hitherto surrounded the institution of bankruptcy cannot but have been diminished by the prospect of a finite, and relatively short, interruption of the individual’s normal legal status.

It may nevertheless be questioned whether the present law has succeeded in its commendable objective of mitigating the plight of the ‘honest but unfortunate’ debtor only at the expense of providing enhanced opportunities for the ‘amoral calculator’ to inflict considerable social and commercial harm at comparatively small personal cost and inconvenience. By reducing the operation of automatic discharge to so short a period as 12 months, regardless of the scale or circumstances of the bankruptcy itself, with the proviso that the bankrupt avoids provoking the trustee into taking steps to stop the clock, as it were, the law has placed those charged with the task of maintaining adequate standards of protection for the public interest under considerable pressure to evaluate the merits of the bankrupt’s pre-adjudication conduct within the brief time available before an automatic discharge will take effect. Although ... a procedure has been created to enable a bankrupt to be subjected to post-discharge restrictions for up to 15 years, an application for the imposition of a bankruptcy restrictions order can only be made after one year from the commencement of bankruptcy with the permission of the court. If the latest legislative dispensation is seen as signalling an abandonment of past policies based on reassuring creditors that the law was designed to deal with parties on the basis of their respective merits, there is a danger of progressive erosion of social attitudes towards the responsible use of credit, including respect for the legal and moral obligations owed by debtors to creditors, to the extent that bankruptcy could in time be viewed as a mere rite of passage, or formative experience, carrying little or no connotation of moral opprobrium. The fact that since the entry into force of the 1-year discharge period in April 2004 the annual statistics for the bankruptcies have soared to unprecedented levels, considered

²²⁷ *Ibid.* In this regard, see the discussions regarding the equality principle within the realm of South African law which basically entails that those who are similarly situated should be similarly treated; ch 1 par 1.1, ch 3 par 3.5 and ch 4 par 4.4. This begs the question as to whether this principle would be applicable to periods under different statutory insolvency procedures. Furthermore, international principles and guidelines caution against the perception that an insolvency procedure provides an easy way out; ch 2 par 2.7.

²²⁸ Fletcher *The law of insolvency* 363–364.

in conjunction with the very high levels of personal indebtedness now prevalent among the UK population at large, may be indicative, in part at least, that such transformation is already under way.

Section 282 sets out the court's power to annul a bankruptcy order.²²⁹ Annulment is competent where it appears to the court that the bankruptcy order should not have been made²³⁰ or where, to the extent required by the rules,²³¹ the bankrupt's debts and expenses in relation to the procedure were paid or security has (to the satisfaction of the court) been provided therefor.²³² An annulment order may be made irrespective of whether or not the bankrupt has already been discharged from bankruptcy.²³³ Where the court annuls a bankruptcy order in terms of sections 282, 261 or 263D²³⁴

- (a) any sale or other disposition of property, payment made or other thing duly done, under any provision in this Group of Parts, by or under the authority of the official receiver or a trustee of the bankrupt's estate or by the court is valid, but
 - (b) if any of the bankrupt's estate is then vested, under any such provision, in such a trustee, it shall vest in such person as the court may appoint or, in default of any such appointment, revert to the bankrupt on such terms (if any) as the court may direct;
- and the court may include in its order such supplemental provisions as may be authorised by the rules.

Paragraphs 10 to 12 of schedule 4A set out the effect of the annulment of a bankruptcy order on bankruptcy restriction orders or undertakings. Where the annulment was ordered on the basis of section 282(1)(a) or (2) any bankruptcy restriction order, interim order or undertaking shall also be annulled. Also, no new restriction or interim orders may be made and no new undertaking may be accepted.²³⁵ However, where a bankruptcy order is annulled in terms of sections 261, 263D or 282(1)(b), bankruptcy restriction orders, interim orders or undertakings in respect of the bankruptcy shall not be affected by the annulment. Furthermore, where an application for a restriction order was instituted before annulment the court

²²⁹ See also ch 21 of pt 6 of the rules. In South Africa, both provisional and final sequestration orders may be rescinded. However, legislation does not set specific grounds therefor; ch 3 par 3.3.1.

²³⁰ S 282(1)(a).

²³¹ See r 6.211.

²³² S 282(1)(b).

²³³ S 282(3).

²³⁴ S 282(4). See par 7.4.1 as regards ss 261 and 263D.

²³⁵ Par 10.

may make the order and similarly, where an undertaking was offered before the annulment, the secretary of state may accept same. However, an application for a restriction order or interim order may not be instituted after annulment.²³⁶

7.4 Alternatives to bankruptcy: Statutory procedures

7.4.1 Individual voluntary arrangement

The process is regulated in part 8 of the Act and part 5 chapters 1 to 15 of the first group of parts of the rules provide for further procedural matters. The procedure is reliant on the courts,²³⁷ but (save for a cram down) cannot generally be imposed upon parties as it is contractual in nature.²³⁸ Spooner therefore describes the procedure as ‘a statutory agreement entered into by a debtor with her creditors for the settlement of her debts’.²³⁹ It offers an ‘earned fresh start’²⁴⁰

in which debtors receive a partial discharge of past indebtedness accompanied by the prospect of wider financial rehabilitation in return for repaying what they can reasonably afford from present and future income over a predictable time period.

Steyn notes that the process is regularly employed to avert the sale of a home in bankruptcy proceedings.²⁴¹

The procedure is generally invoked by debtors²⁴² and specifically those who intend to make a proposal,²⁴³ for a composition in satisfaction of their debts²⁴⁴ or a scheme of arrangement of their affairs,²⁴⁵ to creditors. The proposal may involve assets,

²³⁶ Par 11.

²³⁷ The South African statutory composition is not reliant on the courts and the proposed pre-liquidation composition will also circumvent court involvement; ch 3 par 3.4 and ch 5 par 5.2.

²³⁸ It is for this reason that the procedure cannot be compared with the South African repayment plan procedures, namely, the administration and debt review procedures; ch 4 para 4.2 and 4.3.

²³⁹ Spooner *Personal insolvency law* 90.

²⁴⁰ Walters 2009 *Int Insolv Rev* 8.

²⁴¹ Steyn 2012 *De Jure* 641–642.

²⁴² S 253(3). Where the debtor is an undischarged bankrupt, an application for an IVA may also be made by the trustee of the estate or the official receiver; s 253(3)(a). Where the debtor applies for such under these circumstances, he must give the official receiver and the trustee notice of the proposal to creditors; s 253(4). As was mentioned on various occasions above, the Insolvency Act pays attention to the interplay between the different statutory measures.

²⁴³ See rr 5.2–5.6 as regard the preparation of the debtor’s proposal.

²⁴⁴ A composition is described by Fletcher (*The law of insolvency* 51) as a situation where the debtor personally retains, or resumes, control of his assets and agrees to pay a certain sum to his creditors from the proceeds accruing to him.

²⁴⁵ A scheme of arrangement is described by Fletcher (*Ibid*) as involving the debtor’s making over his assets to a trustee who thereafter administers them in accordance with the terms of the scheme.

income or both.²⁴⁶ McKenzie Skene and Walters observe that salaried homeowners generally need to release some equity and make income contributions whereas debtors with surplus income but no assets need to offer sufficient payments to convince creditors to agree to the plan.²⁴⁷ A debtor needs to make use of an insolvency practitioner in this regard and is responsible for his fees. As insolvency practitioners are involved, IVAs are subject to court regulation and oversight.²⁴⁸ Ramsay observes that ‘entrepreneurial insolvency professionals’ transformed the procedure ‘into a routinized method of processing profitably large numbers of individuals with consumer debts’.²⁴⁹ The procedure acts as an alternative to bankruptcy and is generally used to avoid bankruptcy²⁵⁰ and its restrictions.²⁵¹ However, it is also competent once a bankruptcy has been applied for and even after a bankruptcy order was granted.²⁵² Both of these instances are referred to as voluntary arrangements and are initiated by way of an application to court²⁵³ for an interim order.²⁵⁴ The proposal must nominate a person to act as trustee or to otherwise supervise the implementation thereof. Such a person must be qualified to act as an insolvency practitioner²⁵⁵ or be authorised to act as a nominee as regards voluntary arrangements.²⁵⁶ Fletcher notes that a discharge is generally agreed upon²⁵⁷ which renders the procedure ‘a tool of debt relief’.²⁵⁸ However, ‘the standard market expectation among institutional creditors ... is that the IVA will run for at least

²⁴⁶ McKenzie Skene and Walters 2006 *Am Bankr LJ* 484.

²⁴⁷ *Idem* 485.

²⁴⁸ *Ibid.*

²⁴⁹ Ramsay 2012 *J Consum Policy* 430.

²⁵⁰ McKenzie Skene and Walters 2006 *Am Bankr LJ* 485.

²⁵¹ See Walters 2009 *Int Insolv Rev* 17.

²⁵² Fletcher *The law of insolvency* 50. See also McKenzie Skene and Walters 2006 *Am Bankr LJ* 485. For this reason, amongst others, the procedure may be compared with both the statutory composition (which is competent after a sequestration order was obtained) and the proposed pre-liquidation composition (which is intended as an alternative to sequestration or liquidation proceedings) in South African law; see ch 3 par 3.4 and ch 5 par 5.2.

²⁵³ The court to which the application is made is the one to which the debtor may petition for his own bankruptcy; see ss 373, 374 and 375 and r 5.8; see also Fletcher *The law of insolvency* 52. An application may not be made where a bankruptcy petition was made by the debtor and while it is still pending if the court has appointed an insolvency practitioner to inquire into the debtor's affairs and to report to it; s 253(5).

²⁵⁴ Ss 252(1) and 253(1). See pt 5 ch 3 of the rules as regards the application for an interim order and related matters.

²⁵⁵ Spooner notes that accountants or lawyers generally fulfil this function; Spooner *Personal insolvency law* 90.

²⁵⁶ S 253(2).

²⁵⁷ Fletcher *The law of insolvency* 51.

²⁵⁸ McKenzie Skene and Walters 2006 *Am Bankr LJ* 485.

5 years'.²⁵⁹ The process can be divided into two parts. The first relates to an interim order and resorts under the heading 'moratorium for insolvent'.²⁶⁰ The second, under the heading 'consideration and implementation of debtor's proposal', relates to a final order.²⁶¹

Courts generally have a discretion as to whether an interim order should be made and in this regard it is suggested that the ultimate consideration relates to whether the proposal is 'serious and viable'.²⁶² However, a court may only make an interim order if it is satisfied²⁶³

- (a) that the debtor intends to make a proposal under this part;
- (b) that on the day of the making of the application the debtor was an undischarged bankrupt²⁶⁴ or was able to make a bankruptcy application;
- (c) that no previous application has been made by the debtor for an interim order in the period of 12 months ending with that day;²⁶⁵ and
- (d) that the nominee under the debtor's proposal is willing to act in relation to the proposal.

Whilst the application is pending the court may bar the levying of any distress on the debtor's property or its subsequent sale (or both) and order the stay of any action, execution or other legal process against the debtor or his property.²⁶⁶ Any court in which proceedings are pending may also, upon proof of an application in terms of section 253, order such a stay or allow proceedings to continue on conditions that it may deem fit.²⁶⁷ However, an automatic moratorium only becomes effective later – when an interim order has been granted.²⁶⁸ During an interim order's effective period²⁶⁹

²⁵⁹ Walters 2009 *Int Insolv Rev* 18. The World Bank *Report* considers any repayment period beyond five years as irresponsible from a social point of view; 85–86 and 135. See also ch 2 par 2.7.

²⁶⁰ Ss 252–257.

²⁶¹ Ss 258–263.

²⁶² Fletcher *The law of insolvency* 57.

²⁶³ S 255(1). Unlike the proposed South African pre-liquidation composition, no monetary threshold is set; see ch 5 par 5.2 as regards the South African position.

²⁶⁴ For a discussion of voluntary arrangements subsequent to adjudication see Fletcher *The law of insolvency* 69–72.

²⁶⁵ The proposed South African pre-liquidation composition may only be invoked once every six months; ch 5 par 5.2.

²⁶⁶ S 254(1)(b). No landlord or other person to whom rent is payable may, save with leave of the court, exercise his rights of forfeiture by peaceable re-entry as a result of the debtor's failure to comply with a term or condition of his tenancy; s 254(1)(a).

²⁶⁷ S 254(2).

²⁶⁸ See s 255(3)–(5) as regards orders that the court may make where the debtor is an undischarged bankrupt. International guidelines favour the position where a moratorium on debt

Footnote continues on next page

- (a) no bankruptcy petition relating to the debtor may be presented or proceeded with,
 - (aa) no landlord or other person to whom rent is payable may exercise any right of forfeiture by peaceable re-entry in relation to premises let to the debtor in respect of a failure by the debtor to comply with any term or condition of his tenancy of such premises, except with the leave of the court; and
- (b) no other proceedings, and no execution or other legal process, may be commenced or continued and no distress may be levied against the debtor or his property except with the leave of the court.

An interim order will generally only stay effective for a period of fourteen days beginning with the day after the one on which the interim order was made.²⁷⁰ Within this period the nominee must submit a report²⁷¹ to the court on whether, in his opinion, the proposal 'has a reasonable prospect of being approved and implemented,'²⁷² and a meeting between the debtor and creditors should be summoned to consider the proposal.²⁷³ If he is of the opinion that such a meeting should proceed the report should set out the date, time, and place thereof.²⁷⁴ Where the court is satisfied that a meeting should be summoned, it shall, to enable the consideration of the debtor's proposal and as it deems fit, direct the extension of the interim order's effective period.²⁷⁵ The court may also discharge the interim order if, on application by the nominee, it is satisfied that the debtor did not comply with his obligation to enable the nominee to prepare his report or where for any other reason

enforcement becomes effective once an application is lodged; ch 2 par 2.7. The proposed pre-liquidation composition in South Africa suggests that a moratorium should become effective once a date for the hearing has been determined; ch 5 par 5.2.

²⁶⁹ S 252(2).

²⁷⁰ S 255(6). The court may, on application by the nominee, extend the period for which the interim order is effective to enable him to prepare his report; s 256(4).

²⁷¹ The debtor must provide the nominee with documentary details relating to the voluntary arrangement which he is proposing as well as a statement of his affairs to enable the nominee to prepare his report; s 256(2) and pt 5 ch 2 of the rules. See r 5.5(3) as regards the statement of affairs. See r 5.11 for details of the nominee's report on the proposal. The court may, on application by the debtor where the nominee has failed to submit the report or died or on application by the debtor or the nominee in instances where it would be impracticable or inappropriate for the nominee to continue, order that the nominee be replaced by a qualified insolvency practitioner or a person who is authorised to act as nominee as regards voluntary arrangements; s 256(3). Where a debtor has made the application in instances where the nominee failed to submit a report, the court may order that the interim order shall continue or be renewed for a period determined by the court; s 256(3A).

²⁷² S 256(1)(a).

²⁷³ S 256(1)(aa). See pt 5 ch 5 of the rules regarding the creditors' meeting.

²⁷⁴ S 256(1)(b).

²⁷⁵ S 256(5).

it would not be appropriate to summon a meeting for the consideration of the proposal.²⁷⁶

Due to the costs involved in obtaining an interim order, and therefore also the moratorium, greater flexibility was brought about by the introduction of section 256A which enables the debtor to make a proposal without first applying for an interim order.²⁷⁷ The section therefore applies where a debtor intends to make a proposal, but where an interim order has not been made and is not pending.²⁷⁸ In such instances and where the nominee is of the opinion that the debtor is either an undischarged bankrupt or that he may apply for his bankruptcy,²⁷⁹ he (the nominee) must within fourteen days²⁸⁰ submit a report²⁸¹ to creditors stating whether, in his opinion, the proposal has a reasonable prospect of approval and implementation²⁸² and whether a meeting of creditors should be summoned to consider the proposal²⁸³ as well as the date, time and place of the proposed meeting.²⁸⁴

Where a meeting should be summoned, either as reported to the court in terms of section 256 or to creditors in accordance with section 256A, the nominee shall summon same for the date, time and place proposed in the report.²⁸⁵ In this regard every creditor of whose claim and address the nominee is aware should be summoned.²⁸⁶

²⁷⁶ S 256(6).

²⁷⁷ Fletcher *The law of insolvency* 72–73. See pt 5 ch 4 of the rules as regards cases where no interim order is needed. S 256A reduces costs which is one of the attributes that international guidelines suggest would potentially enhance the probability of successful negotiations; ch 2 par 2.7.

²⁷⁸ S 256A(1). If the debtor is an undischarged bankrupt, he must give notice of the proposal to the official receiver and to the trustee; s 256A(1)(b).

²⁷⁹ S 256A(3).

²⁸⁰ Or a longer period allowed by the court. S 256A(5) provides that the nominee may apply to the court to extend the period. S 256A(4) contains provisions similar to s 256(3) in relation to instances where the nominee fails to submit his report, dies or where it is impracticable or inappropriate for the nominee to continue.

²⁸¹ In this regard the debtor must provide the nominee with a document setting out the terms of the proposal and a statement of affairs setting out particulars as regards his creditors, debts, liabilities and assets as well as other prescribed information; s 256A(2).

²⁸² S 256A(3)(a).

²⁸³ S 256A(3)(b).

²⁸⁴ S 256A(3)(c).

²⁸⁵ S 257(1). Unless, in the event that s 256 is applicable, the court directs otherwise.

²⁸⁶ S 257(2). Every person who is a creditor of the bankrupt in relation to bankruptcy debt and who would have been such had the bankruptcy commenced on the day on which the notice is provided, is a creditor of an undischarged bankrupt; s 257(3).

At the meeting, which must be conducted in accordance with the rules,²⁸⁷ the summoned creditors shall decide whether the proposed voluntary arrangement should be approved²⁸⁸ and modifications thereto may only be effected with the debtor's consent.²⁸⁹ A majority in excess of three quarters in value of creditors present and voting is required.²⁹⁰ The fact that dissenting creditors are bound to the IVA constitutes a key feature.²⁹¹ Secured creditors will not be affected by the proposal, except where they agree thereto.²⁹² Furthermore and without preferential creditors' concurrence, terms under which preferential debts would be deprived of their status may not be approved.²⁹³

Once the meeting has been concluded, the chairman, which is usually the nominee,²⁹⁴ must notify prescribed persons as well as the court (in the event that the meeting was in pursuance to a report to the court)²⁹⁵ of its outcome.²⁹⁶ Where the meeting did not approve the voluntary arrangement, the court may discharge the interim order.²⁹⁷

²⁸⁷ S 258(6).

²⁸⁸ S 258(1).

²⁸⁹ S 258(2). Such modifications may have the effect of conferring the proposed functions of the nominee on another qualified person, but may not include a modification which will render the proposal something other than a proposal in terms of this part of the Act; s 258(3).

²⁹⁰ R 5.23(1).

²⁹¹ Also dissenting creditors are bound even if they did not obtain notice of the meeting. This element strengthens the stability of the procedure. Even though this stability is attained by dispensing with one of the elements of due process in that persons are bound by the outcome of a meeting of which they were not aware, or could not have been aware, it may be 'defended on the basis that it seeks to promote the greatest good for the greatest number'. Furthermore, creditors who can show a real ground for challenging the decision are allowed a special extension of time to challenge the decision; see below and Fletcher *The law of insolvency* 64. The procedure's feature, that creditor passivity are not allowed to obstruct agreements, is on par with international principles and so is the cram down as it has the potential to enhance the success of arrangements. However, the required percentage is very high; ch 2 par 2.7. The South African statutory composition requires a creditors' vote of at least 75% in value and in number of those who have proven claims against the estate. The 2015 Insolvency Bill proposes a mere majority in number and two-thirds in value of concurrent creditors who vote; ch 3 par 3.4. Also, the proposed pre-liquidation composition requires a majority in number and two-thirds in value vote. It provides that the composition binds those who received notice of or who have appeared at the hearing; ch 5 par 5.2.

²⁹² S 258(4). The general protection of secured creditors' rights is in accordance with international principles; ch 2 par 2.7. Both the South African statutory composition and the proposed pre-liquidation composition respect the rights of secured creditors; ch 3 par 3.4 and ch 5 par 5.2.

²⁹³ S 258(5). The South African statutory composition as well as the proposed pre-liquidation composition contain similar provisions; ch 3 par 3.4 and ch 5 par 5.2.

²⁹⁴ R 5.19.

²⁹⁵ See s 256(1)(aa).

²⁹⁶ S 259(1).

²⁹⁷ S 259(2).

The effect of the meeting's approval of the proposed voluntary arrangement is²⁹⁸ that it is effective as if it was made by the debtor at the meeting²⁹⁹ and binds every person who was, in accordance with the rules, entitled to vote or would have been entitled if he had notice of the meeting.³⁰⁰ An interim order in force prior to the end of a 28-day period, which begins with the day on which the report as regards the creditors' meeting was made to the court, ceases to have effect at the end thereof.³⁰¹ However, an approved arrangement constitutes an effective bar to enforcement of debt by a creditor bound to it, although it does not generally affect secured creditors.³⁰² Where proceedings in relation to a bankruptcy petition were stayed by an interim order which so ceases, the petition is, unless the court orders otherwise, deemed to have been dismissed.³⁰³ If the meeting has approved the proposed voluntary arrangement of an undischarged bankrupt, the court shall, on application by the debtor or the official receiver,³⁰⁴ annul the bankruptcy.³⁰⁵

The procedure provides for a challenge of the meeting's decision, on application to court and within a 28-day period, which commences on the day on which the report of the meeting was made to the court,³⁰⁶ on the basis that a creditor's interests were unfairly prejudiced or that there had been a material irregularity as regards the meeting.³⁰⁷ The debtor, a person who was entitled to vote at the meeting (or would have been entitled had he received notice), the nominee or, where the debtor is an

²⁹⁸ S 260(1).

²⁹⁹ S 260(2)(a).

³⁰⁰ S 260(2)(b). This element of the procedure is in line with international guidelines as regard informal arrangements as was noted above; ch 2 par 2.7.

³⁰¹ S 260(4).

³⁰² Fletcher *The law of insolvency* 64–65.

³⁰³ S 260(5).

³⁰⁴ Such application is not competent before the period during which an approval may be challenged has lapsed; whilst such an application is pending; or while an appeal in respect thereof is pending; s 261(3).

³⁰⁵ See s 261(1) and (2). The court may provide further direction as regards the conduct of the bankruptcy and the administration of the estate as it deems appropriate for facilitating the implementation of the approved arrangement; s 261(4). See also pt 5 chs 8, 9, 10 and 11 of the rules as regards annulment of the bankruptcy order. The South African statutory composition does not provide for annulment or rescission of the sequestration, but the insolvent may immediately apply for his rehabilitation if 50 cents in the rand was paid in respect of proven claims or security has been provided therefor. The 2015 Insolvency Bill does away with the 50 cents requirement in relation to early eligibility for rehabilitation which would render more debtors eligible for an early discharge; ch 3 par 3.4.

³⁰⁶ S 262(3)(a). Where a person was not given notice of the meeting, after a period of 28 days from the day on which he became aware that a meeting has taken place; s 262(3)(b).

³⁰⁷ S 262(1) and (3).

undischarged bankrupt, the trustee or the official receiver may bring the application.³⁰⁸ The court may revoke or suspend the meeting's approval and direct a person to summon a further meeting to consider a revised proposal or, where there has been a material irregularity, to reconsider the original proposal.³⁰⁹

Where a voluntary arrangement has been approved and has taken effect,³¹⁰ the nominee becomes the supervisor who must implement the arrangement.³¹¹ Any person who is dissatisfied with any act, omission or decision of the supervisor may apply to the court that may confirm, reverse or modify any act or decision. It may also provide the supervisor with direction or make any other appropriate order.³¹² The supervisor may also apply to the court for directions.³¹³ A court may further replace a supervisor or fill a vacancy in such regard.³¹⁴ However, although the courts remain involved Fletcher comments that modern law as regards voluntary arrangements is based on the principle that the procedure should (where possible) resort under the control of a duly qualified insolvency practitioner who can be trusted to competently administer the process without close or persistent supervision of the court or insolvency service.³¹⁵

The arrangement only protects the debtor as long as he does not default thereon. Once he defaults, and as was discussed above,³¹⁶ a bankruptcy application becomes possible.³¹⁷

In the event that an arrangement is fully implemented or terminated, the supervisor must provide the debtor, all bound creditors, the secretary of state and the court with

³⁰⁸ S 262(2).

³⁰⁹ S 262(4). For further procedural matters see 262(5)–(8).

³¹⁰ S 263(1).

³¹¹ S 263(2). The legal status of a supervisor has not been defined and largely depends on the arrangement. Nevertheless, where his primary function is to realise assets and distribute proceeds to creditors, his role is that of a trustee; see Fletcher *The law of insolvency* 67 and authority cited there. See pt 5 ch 6 of the rules as regards the implementation of the arrangement.

³¹² S 263(3).

³¹³ S 263(4).

³¹⁴ S 263(5)–(6).

³¹⁵ Fletcher *The law of insolvency* 67.

³¹⁶ Par 7.3.

³¹⁷ See s 264(1)(c) read together with s 276 and Fletcher *The law of insolvency* 68–69 and 150 *et seq.*

a notice to that effect together with a report as to the implementation.³¹⁸ There are no further statutory provisions as regards this concluding stage of the proceedings.³¹⁹

The procedure provides that a debtor commits an offence if he makes a false representation or fraudulently does or omits to do something in order to obtain the approval of creditors even if the proposal is not approved.³²⁰ It also provides for procedural matters regarding the prosecution of delinquent debtors in instances where a voluntary surrender has been approved and where it appears to the nominee or supervisor that the debtor is guilty of an offence regarding the rearrangement for which he is criminally liable.³²¹

Sections 263A to 263G³²² provide for a 'fast track voluntary arrangement', where the debtor is an undischarged bankrupt who wants to make a proposal to his creditors and where the official receiver would act as nominee. However, Fletcher is of the opinion that there may be limited motivations to utilise this procedure as a bankrupt can obtain a discharge after one year.³²³

Spooner notes that English policymakers have, in the mid-2000s, pursued the possibility of reforming the IVA procedure to found it as the primary consumer debtor remedy and to facilitate more concessions by creditors. However, such endeavours were unsuccessful.³²⁴

Finally, it has to be mentioned that standard conditions for IVAs were set up by creditors and insolvency practitioners.³²⁵ A protocol for treating standard cases was

³¹⁸ R 5.34.

³¹⁹ Fletcher *The law of insolvency* 68.

³²⁰ S 262A(1) and (2). A person guilty of such an offence is liable to imprisonment, a fine or both; s 262A(3). These provisions attempt to curb moral hazard; Spooner *Personal insolvency law* 90–91.

³²¹ S 262B.

³²² These sections were introduced into the Insolvency Act 1986 by s 264 and sch 22 of the Enterprise Act 2002. See also pt 5 ch 7 of the rules.

³²³ Fletcher *The law of insolvency* 74.

³²⁴ Spooner *Personal insolvency law* 91.

³²⁵ See Association of Business Recovery Professionals *Standard conditions for individual voluntary arrangements* <http://bit.ly/1NqbXt9> (accessed 21 August 2015). The document was last revised in January 2013.

also developed.³²⁶ Although Spooner notes that guidelines as regards living expenses are regularly drafted, these are not publically accessible.³²⁷ The protocol was developed due to a concern that the full voluntary arrangement process was not suited to cases of consumer debtors with limited means but who receive regular income and can provide for themselves and have a surplus left to service debt. Major concerns were that the costs involved in voluntary arrangements as well as the ability of large financial institutions to bar the adoption of proposals serve as disincentives to utilise the process. Therefore, and after consultation, a voluntary agreement was reached on a protocol providing a 'standard framework for dealing with straightforward consumer IVA'. It first became effective in February 2008 and the latest version is the 'IVA Protocol 2014'. These procedures remain subject to the Act, but the agreed approach to 'straightforward' cases minimises costs and uncertainties. It may be used by homeowners (and non-homeowners) and may prohibit the outright forced sale of the home. Although creditors' right to vote for or against the proposal remains, creditors should wherever possible accept the terms unless there are sound and revealable reasons not to do so.³²⁸

7.4.2 Debt relief order

The DRO procedure is modelled on the New Zealand no asset procedure³²⁹ and is regulated by part 7A of the Insolvency Act which consists of sections 251A to 251X.³³⁰ The procedure was introduced by the Tribunals, Courts and Enforcement Act³³¹ and became fully effective on 6 April 2009.³³² Part 5A of the Insolvency Rules, consisting of rules 5A.1 to 5A.27, provides for further procedural matters.

³²⁶ See The insolvency service *Individual voluntary arrangement (IVA) protocol* <http://bit.ly/1h03wqK> (accessed 21 August 2015).

³²⁷ Spooner *Personal insolvency law* 90.

³²⁸ *Idem* 75–77.

³²⁹ See McKenzie Skene and Walters 2006 *Am Bankr LJ* 501. The authors (n184) submit that [i]n New Zealand, the objective is to channel NINAs away from bankruptcy, which is regarded as an excessively punitive response to the problems of subsistence-level debtors and welfare recipients ... By contrast, in England and Wales, the need for bankruptcy administration to remain self-financing, manifested in the government's refusal to countenance means-tested exemption from the requirement to pay the OR's deposit, is perhaps the most significant driver behind the establishment of a separate scheme.

See ch 6 par 6.5.3 for an in-depth discussion of the no asset procedure in New Zealand.

³³⁰ See McKenzie Skene and Walters 2006 *Am Bankr LJ* 500–503 for a discussion of the procedure.

³³¹ S 108(1) and sch 17.

³³² SI 2009/382, a 2(b). See McKenzie Skene and Walters 2006 *Am Bankr LJ* 500–503 for a discussion of the run-up to the enactment of the procedure.

Before the procedure was introduced in England and Wales, NINA debtors did not have a form of recourse as they were not in a position to make arrangements with their creditors and therefore the IVA,³³³ CCAO³³⁴ and informal debt resolution³³⁵ measures were not at their disposal. Furthermore, such debtors could not enter the bankruptcy procedure as they were not in a position to pay the required fees.³³⁶ However, NINA debtors often entered the CCAO procedure only to default thereon.³³⁷

Fletcher describes the purpose of the procedure as follows:³³⁸

The objective of the new procedure is to provide debt relief for people who owe relatively little, have no income and no assets to repay what they owe, and who cannot afford the cost of petitioning for their own bankruptcy adjudication.

The procedure essentially allows an individual who is unable to pay his debts to (in electronic form)³³⁹ apply³⁴⁰ to the official receiver, through an approved intermediary,³⁴¹ for a DRO as regards his qualifying debt.³⁴²

³³³ See par 7.4.1.

³³⁴ See par 7.4.3.

³³⁵ See par 7.5.

³³⁶ See par 7.3.2. Department for Constitutional Affairs *A choice of paths* 16–17 <http://bit.ly/1TXAQAA> (accessed 21 August 2015).

³³⁷ Department for Constitutional Affairs *A choice of paths* 16 <http://bit.ly/1TXAQAA> (accessed 21 August 2015).

³³⁸ Fletcher *The law of insolvency* 386.

³³⁹ See r 5A.4.

³⁴⁰ The application should include details as regards debts at the time of the application, security held in respect of such debts and other information as may be prescribed; s 251B(2). See further r 5A.3 regarding required information. An application is regarded as having been made once it has been submitted to the official receiver and the required fee has been settled; s 251B(4). See s 251J and r 5A.17 regarding the debtor's duties to assist the official receiver once an application has been made. He has to, amongst others, supply the official receiver with information, attend meetings and inform the official receiver of errors or omissions in information supplied or any change in circumstances between the application and determination dates. He must also, once a DRO is made, inform the official receiver as soon as reasonably practicable of an increase in income or a property gain. The same applies once he becomes aware of an error or omission as regards supplied information.

³⁴¹ See s 251U in relation to approved intermediaries. Specifically refer to s 251U(7) which provides that such intermediaries may not charge any fee in connection with an application for a DRO. Approved intermediaries are not liable for damages in connection with an act or omission in relation to an application for a DRO except if such act or omission was in bad faith; s 251U(8) and (9). See further r 5A.5 regarding the functions and duties of approved intermediaries.

³⁴² See s 251A(1) and 251B(1). According to s 251A(2) 'Qualifying debt' is a debt which
(a) is for a liquidated sum payable either immediately or at some certain future time; and
(b) is not an excluded debt.

An 'excluded debt' includes fines in relation to an offence and any obligation in terms of an order made in family proceedings or any obligation arising under a maintenance assessment in terms of the Child Support Act 1991; an obligation in terms of a confiscation order in relation to s 1 of

Footnote continues on next page

Secured debt is not affected by the procedure.³⁴³ The courts are not involved in the procedure as it 'falls outside of the court's functions of dispute resolution and enforcement regulation'.³⁴⁴ It is also too expensive to involve the courts and the insolvency service has the expertise to offer a more comprehensive system and may refer cases for investigation where appropriate.³⁴⁵ As the procedure does not involve assets and does not require a default investigation into the debtor's affairs, only a moderate fee is needed to cover administrative costs.³⁴⁶

A DRO will only be granted if the following criteria are met:³⁴⁷

- a. The debtor should have total liabilities of less than £15 000.
- b. The debtor should have a maximum surplus income of £50 per month after paying normal household expenses.³⁴⁸
- c. The debtor should have assets, other than excluded assets,³⁴⁹ of no more than £300.³⁵⁰ If the debtor owns a motor vehicle it may not be worth more than £1 000.³⁵¹

the Drug Trafficking Offences Act 1986 or s 1 of the Criminal Justice (Scotland) Act 1987 or s 71 of the Criminal Justice Act 1988 or pts 2, 3 or 4 of the Proceeds of Crime Act 2002; debt or liability in relation to a student loan; liability for damages for negligence, nuisance or breach of a statutory, contractual or other duty or to pay damages in terms of pt 1 of the Consumer Protection Act 1987 'being in either case damages in respect of the death of or personal injury ... to any person'; r 5A.2.

³⁴³ S 251A(3) and 251G(5). This element is in line with international principles and guidelines; ch 2 par 2.7.

³⁴⁴ The reduction of court involvement is in line with international principles and guidelines; ch 2 par 2.7.

³⁴⁵ Department for Constitutional Affairs *A choice of paths* 17 <http://bit.ly/1TXAQAA> (accessed 21 August 2015).

³⁴⁶ *Idem* 18. The official receiver's fee is set at £90 which may be paid in instalments. However, the official receiver would not consider an application before the fee has been paid in full. See s 251B(4)(b) read together with s 251C(4)(a) of the Insolvency Act 1986. International principles and guidelines provide that costs should not pose an access barrier which is heeded as regards the minimal DRO fee; ch 2 par 2.7.

³⁴⁷ See sch 4ZA and Gov.uk *Options for paying off your debt* <http://bit.ly/1V6f2k8> (accessed 21 August 2015). Where a debtor does not have access to other measures and cannot satisfy the DRO entry requirements he will be excluded from the broader system which is contrary to international principles and guidelines that lobby for access for all honest but unfortunate debtors; ch 2 par 2.7. However, a total exclusion from all measures will only arise in the absolute minority of cases especially since the bankruptcy procedure does not pose substantive access requirements; par 7.3.2.

³⁴⁸ See r 5A.8.

³⁴⁹ See r 5A.10. Assets that the official receiver should disregard include tools, books and items or equipment necessary for employment, business or vocation; clothing, bedding, furniture, household equipment necessary for domestic needs; and some forms of tenancy.

³⁵⁰ See r 5A.9 as regards the determination of the value of the debtor's property; r 5A.10(1).

³⁵¹ R 5A.10(1)(b) and (4)(a). These thresholds are very low. In this respect higher levels of exemptions will result in increased access.

- d. The debtor should, within the past three years, have lived or worked in England and Wales.
- e. The debtor should not have applied for a DRO within the past six years.³⁵²

The official receiver must consider the application³⁵³ and in this regard may only refuse a debtor's application on specific grounds set out in the Act and must refuse it on the basis of others. If he refuses the application, he must provide reasons therefor.³⁵⁴ Reasons for which he may refuse the application are that it does not meet the requirements for making the application as provided for in section 251B; queries raised with the debtor have not been satisfactorily answered within the time allowed by the official receiver;³⁵⁵ the debtor has made false representations or omissions in relation to the application, information or documents in terms thereof;³⁵⁶ or where he (the official receiver) is not satisfied that every condition set out in part 2 of schedule 4ZA³⁵⁷ has been met. Reasons for which the official receiver must refuse the application are where he is not satisfied that the debtor cannot pay his debts; at least one of the debts was a qualifying debt when the application was made; or every condition set out in part 1 of schedule 4ZA³⁵⁸ has been met.³⁵⁹ Such conditions, amongst others, include that the debtor is not an undischarged bankrupt or subject to an interim order or voluntary arrangement in terms of part 8 of the Act.³⁶⁰

³⁵² See sch 4ZA(5).

³⁵³ See s 251D relating to presumptions applicable to the determination of the application which basically entails that the official receiver may accept certain facts as the truth without going to lengths to verify same, although some verification is needed in some instances. In this respect see also r 5A.7. The general exclusion of creditor participation coincides with international principles and guidelines; ch 2 par 2.7.

³⁵⁴ S 251C(3) and (7). See further r 5A.6 regarding the form, manner and reasons for refusal of an application for a DRO.

³⁵⁵ The official receiver may stay the consideration of the application until he has received answers to queries as regards the application; s 251C(2).

³⁵⁶ S 251C(4).

³⁵⁷ Pt 2 is titled 'Other conditions'. These relate to transactions entered into at undervalue and preferences given during the period between two years prior to the application date and the determination date.

³⁵⁸ Pt 1 is titled 'Conditions which must be met'. These relate to the debtor's connection with England and Wales; his previous insolvency history; bankruptcy petitions; whether a DRO has been made within the previous six years; the limit on the debtor's overall indebtedness, monthly surplus income and property.

³⁵⁹ S 251C(5).

³⁶⁰ See sch 4ZA(2)–(4) which clearly sets out the interplay between the different statutory procedures.

If the official receiver does not refuse the application he must make a DRO³⁶¹ in relation to the specified debts that to his satisfaction were qualifying debts at the date of application.³⁶² Once the official receiver has made the order, it is entered into the register³⁶³ and such date is referred to as the effective date.³⁶⁴ On such date a moratorium commences in relation to the specified qualifying debt.³⁶⁵ In this regard, relevant creditors do not, save with permission of the court and on terms that the court may impose, have any remedy in relation to their debts and may not institute a creditor's petition, any action or other legal proceedings against the debtor.³⁶⁶ Generally, the moratorium will be in force for one year after which qualifying debts will be discharged.³⁶⁷ However, the term may be extended by the official receiver or the court.³⁶⁸ The period may only be extended by the official receiver for the purpose of carrying out or finalising an investigation in terms of section 251K – however, in this regard the court's permission is necessary;³⁶⁹ taking action necessary (which may be as a result of an investigation) in relation to the order; or in instances where a decision was made to revoke the order, to allow the debtor to make the necessary arrangements regarding payments of his debts.³⁷⁰ The official receiver may only extend the moratorium period with three months, but the extension must be made before the original term expires.³⁷¹

As was mentioned above, the discharge does not affect secured debt. It also does not relate to qualifying debt incurred in respect of fraud or fraudulent breach of

³⁶¹ See s 251E as regards further requirements relating to the making of a DRO and r 5A.11 in connection with formal requirements.

³⁶² S 251C(3).

³⁶³ S 251E(4)(b) and s 251W(a). See also r 5A.12(1)(b). Once the order is made the official receiver must notify prescribed persons or entities of prescribed information; r 5A.12 and r 5A.13.

³⁶⁴ S 251E(7).

³⁶⁵ International principles and guidelines favour the position where a moratorium becomes effective once an application is lodged; ch 2 par 2.7.

³⁶⁶ S 251G(1) and (2). If on the effective date a creditor has any such proceeding pending in any court, the court may stay such proceedings or allow them to proceed on terms that it deems appropriate; s 251G(3).

³⁶⁷ S 251H(1) and 251I(1). The relatively wide discharge is in line with international principles and guidelines; ch 2 par 2.7. The one-year period after which an automatic discharge is granted is similar to the position in terms of the bankruptcy procedure; par 7.3.4.

³⁶⁸ S 251H(1)(b). See further r 5A.20.

³⁶⁹ S 251H(3).

³⁷⁰ S 251H(2).

³⁷¹ S 251H(4) and (5).

trust³⁷² and does not release any other person from any liability in respect of which the debtor is released or as surety for the debtor.³⁷³

Creditors' interests are taken into consideration as the debtor is only allowed to apply for a DRO once every six years.³⁷⁴ Provision is also made for creditors, within the period that the moratorium is effective, to object to the making of the order, or to the inclusion of a debt on the list of qualifying debts or details of debt included in the order.³⁷⁵ Such objections are made, within the prescribed period for objections,³⁷⁶ to the official receiver, who must consider the objection and may carry out an investigation in relation thereto.³⁷⁷ The decisions which may be investigated are whether the order should be revoked or amended,³⁷⁸ an application should be made to court,³⁷⁹ or other steps should be taken in relation to the debtor.³⁸⁰

As regards the power of the official receiver to revoke or amend a DRO during the period for which the moratorium is effective, the Act sets out specific grounds under which a revocation is competent.³⁸¹ These are that information supplied by the debtor was incomplete, incorrect or misleading; the debtor has failed to comply with his statutory duties;³⁸² a bankruptcy order has been made in respect of the debtor; the debtor has made a proposal or has notified the official receiver of his intention to do so;³⁸³ or where he should not have been satisfied that the debts specified in the order were qualifying debts or that the conditions specified in schedule 4ZA were met.³⁸⁴

³⁷² S 251I(3).

³⁷³ S 251I(4).

³⁷⁴ See sch 4ZA(5).

³⁷⁵ S 251K(1) and (2) read together with r 5A.14. See r 251K(4) as regards grounds upon which objecting creditors may rely. These include that a bankruptcy order has been made and that the debtor has made a proposal under the IVA procedure.

³⁷⁶ See r 5A.14(3).

³⁷⁷ S 251K(2), (3) and (4). An investigation is competent whilst the moratorium is effective and also after it has come to an end. The official receiver may carry it out in the manner that he deems appropriate and may require any person to provide him with information and assistance in connection therewith; s 251K(6), (7) and (8).

³⁷⁸ Under s 251L. See also r 5A.15 and r 5A.16 for procedural matters.

³⁷⁹ Under s 251M.

³⁸⁰ S 251K(5).

³⁸¹ S 251L.

³⁸² In terms of s 251J.

³⁸³ The latter two grounds address the issue of interplay between statutory debt relief provisions.

³⁸⁴ S 251L(3)–(4).

The DRO may be revoked with immediate effect or from a specified date.³⁸⁵ As far as the possibility of amendment of the DRO is concerned, the official receiver may correct an error or omission, but may not add debts that were not specified in the application for the order.³⁸⁶

As can be gathered from the discussions so far, the DRO procedure is intended to operate with generally no court involvement. However, courts are still involved in exceptional cases, for instance where a creditor applies for the court's permission to commence or further individual enforcement proceedings or petitions for the debtor's bankruptcy.³⁸⁷ Furthermore, as regards court involvement in the DRO procedure, any person who is dissatisfied with an act, omission or decision of the official receiver or an application for a DRO may, at any time,³⁸⁸ apply to court for relief.³⁸⁹ With reference to the official receiver specifically, he may apply to court for directions, or an order relating to any matter in connection with the DRO or the application therefor.³⁹⁰ These may include matters relating to the debtor's compliance with his duties in terms of section 251J.³⁹¹ When such an application is made, the court may extend the period for which the moratorium is in effect in order to consider the application.³⁹² The court has wide and generally non-restrictive discretion regarding the determination of the application. In this regard it may for instance dismiss the application, order an inquiry (by the court) into the debtor's dealings and property,³⁹³ revoke or amend the DRO and negate an act or decision of

³⁸⁵ Which may not be more than three months after the date of the decision; s 251L(5). See s 251L(6) and (7) for further procedural matters.

³⁸⁶ S 251L(8) and (9).

³⁸⁷ See s 251G above.

³⁸⁸ S 251M(4).

³⁸⁹ S 251M(1). See r 5A.19(a) for procedural matters. It is interesting that any person, and not only interested ones, may make such an application. Any application to court in terms of s 251M generally follows the domicile of the debtor; r 5A.21.

³⁹⁰ S 251M(2). See r 5A.19(b) for procedural matters.

³⁹¹ S 251M(3). See the discussion of s 251J above.

³⁹² S 251M(5).

³⁹³ In terms of s 251N. Such an order is competent where the official receiver applies therefor; s 251N(1). It entails a procedure whereby the court may summon persons of interest to appear before the court to provide information and documentation regarding the debtor's dealings and property; s 251N(2) and (3). Where such a person fails to appear without reasonable excuse, the court may issue a warrant of arrest and seizure of records or other documents in such person's possession; s 251N(4), (5) and (6). Any application to court in terms of s 251N generally follows the domicile of the debtor; r 5A.21.

the official receiver.³⁹⁴ However, the court may not amend the DRO by adding qualifying debts that were not specified in the application for the DRO.³⁹⁵ As regards the power to revoke the DRO, such an order may be made before and after the moratorium has come to an end and even on the court's own motion in instances where it has made a bankruptcy order in relation to the debtor.³⁹⁶

The DRO procedure provides that certain actions and omissions of the debtor would constitute an offence.³⁹⁷ The procedure safeguards against debtor misrepresentations and omissions. For instance where such conduct or omission in relation to the application was recklessly or knowingly made it would constitute an offence.³⁹⁸ It would also be an offence where a debtor in respect of whom a DRO is made intentionally fails to comply with a duty in terms of section 251J(5)³⁹⁹ or knowingly or recklessly makes a false representation or omission as regards information to be provided to the official receiver. The same applies to information supplied in relation to the performance of the official receiver's functions in terms of the order.⁴⁰⁰ Under certain circumstances, the concealment or falsification of documents regarding the debtor's affairs, the fraudulent disposal of property⁴⁰¹ and the fraudulent dealing with property⁴⁰² obtained on credit would also constitute an offence.⁴⁰³

Whilst a DRO is in force the debtor is subject to similar restrictions as in bankruptcy. The debtor is for example not allowed to obtain credit over £500⁴⁰⁴ without disclosing to the creditor that he is subject to a DRO. He may also not engage in business

³⁹⁴ S 251M(6).

³⁹⁵ S 251M(8).

³⁹⁶ S 251M(7).

³⁹⁷ See s 251T as regards offences under this part.

³⁹⁸ S 251O(1) and (2). It is immaterial whether the order was made on the basis of the application; s 251O(3).

³⁹⁹ See above.

⁴⁰⁰ S 251O(4). It is immaterial whether the offence is committed during or after the moratorium period and whether or not the order is revoked thereafter; s 251O(5).

⁴⁰¹ For a period of two years before the order was made and whilst the moratorium is effective; s 251Q(1).

⁴⁰² For a period of two years before the order was made up until the determination date; s 251R(3).

⁴⁰³ Ss 251P, 251Q and 251R. Once again, it is immaterial whether or not the DRO is revoked after the conduct took place. However, no offence is committed in relation to conduct after the order is revoked; s 251P(6), s 251Q(5) and s 251R(8).

⁴⁰⁴ S 251S(4) and Gov.uk *Options for paying off your debt* <http://bit.ly/1V6f2k8> (accessed 21 August 2015).

under another name (than the one in terms of which the order was made) without disclosing the name under which the order was made. Such conduct would constitute an offence.⁴⁰⁵

Should it be found that the debtor was dishonest before or during the period of the DRO, the secretary of state or the official receiver could apply to court for a so-called debt relief restriction order which may extend for a period of up to 15 years. The debtor may also agree to a debt restriction undertaking.⁴⁰⁶

Early indications of evidence forming part of a review study conducted by the Department for Business Innovations and Skills record that the DRO model is functioning well and that it has 'a very significant impact on the wellbeing of debtors'. However, there are overwhelming support for an increase in the maximum debt threshold and assets that a debtor may possess when applying for a DRO. Nonetheless, participants are of the opinion that the surplus income threshold should remain at £50 per month.⁴⁰⁷

7.4.3 County court administration orders

The CCAO procedure is regulated by part 6 of the County Courts Act and has been amended and proposed to be amended on several occasions, most recently by the Tribunals, Courts and Enforcement Act.⁴⁰⁸ The latest amendment will probably substitute the existing procedure in future and already forms part of the Act, although it has not been rendered effective as yet.⁴⁰⁹ Sections 112 to 117 set out the prevailing procedure⁴¹⁰ which is only briefly be referred to here as it 'has fallen

⁴⁰⁵ S 251S.

⁴⁰⁶ S 251V and sch 4ZB. The secretary of state must maintain a register of matters relating to DROs, debt relief restriction orders and debt relief restriction undertakings; s 251W. Compare the similar provisions as regards bankruptcy in relation to bankruptcy restriction orders and undertakings; par 7.3.5. Debt relief restriction orders and undertakings heed the international warning against abusive applications; ch 2 par 2.7.

⁴⁰⁷ Department for Business Innovation and Skills *Insolvency proceedings 2* <http://bit.ly/1PDfD9c> (accessed 21 August 2015).

⁴⁰⁸ See s 106 of pt 5 of ch 1 of the Act. See also Fletcher *The law of insolvency* 82.

⁴⁰⁹ For a discussion of the proposed procedure see Fletcher *The law of insolvency* 81–84.

⁴¹⁰ See Department for Constitutional Affairs *Managing multiple debts* <http://bit.ly/1U3XYM> in general and *A choice of paths* 14–15 <http://bit.ly/1TXAQAA> (both accessed 21 August 2015) as well as McKenzie Skene and Walters 2006 *Am Bankr LJ* 487–488 for discussions of the procedure. The discussion in this paragraph is based on the latter source.

largely into disuse⁴¹¹ and holds marginal status – it consequently rarely forms part of personal insolvency policy discussions.⁴¹² McKenzie Skene and Walters submit that many NINA debtors opted for this procedure which was not suited to their needs.⁴¹³ The introduction of the DRO procedure may thus explain the CCAO procedure's increasing redundancy.

Fletcher describes the purpose of the procedure as⁴¹⁴

an alternative to bankruptcy for those individuals whose aggregate debts, and likewise their personal assets, are small, and who also have a regular wage or income from which, over time, their debts may be repaid.

The procedure is court-based and may be utilised by those with multiple debts that do not in total exceed £5 000.⁴¹⁵ One of these debts must be a judgment debt.⁴¹⁶ A debtor must file a request at a county court where an officer determines whether the debtor has sufficient means to service the debts in full within a reasonable timeframe. If the officer is satisfied that it is possible, he will set the amount and frequency of payments and will notify both the debtor and creditors listed in the request. The debtor or creditors may object. Where no objection is lodged, the officer will make a CCAO order. Where an objection is received or where the debtor cannot make full payment within a reasonable time the matter is referred to a district judge. The court may order a discharge.⁴¹⁷ Once a CCAO is granted, a moratorium on debt enforcement becomes effective,⁴¹⁸ no further interest may be charged and the court further manages the debt.⁴¹⁹

⁴¹¹ Spooner *Personal insolvency law* 90 n655. See also McKenzie Skene and Walters 2006 *Am Bankr LJ* 497.

⁴¹² The procedure was barely mentioned by Spooner in his doctoral thesis; Spooner *Personal insolvency law*.

⁴¹³ McKenzie Skene and Walters 2006 *Am Bankr LJ* 501.

⁴¹⁴ Fletcher *The law of insolvency* 81. See also McKenzie Skene and Walters 2006 *Am Bankr LJ* 487.

⁴¹⁵ S 112(1).

⁴¹⁶ *Ibid.*

⁴¹⁷ S 112(6) read together with s 117.

⁴¹⁸ S 114(1). This generally includes a bankruptcy petition; s 112(4).

⁴¹⁹ S 117.

7.5 Informal procedures

Fletcher notes two constructions outside the statutory procedures ‘for bringing about an accommodation between debtor and creditors’⁴²⁰ and mentions that it is much used in practice.⁴²¹ These are informal moratoria and the common law composition.⁴²²

Informal moratoria may entail simple agreements by one or more creditors to grant further credit facilities or an extension of time to discharge liabilities. These arrangements may also be more complex and involve the rescheduling of debts in combination with imposing constraints on the debtor relating to for instance the debtor’s conduct of his business and personal affairs as well as his relations with property. These moratoria will obviously only serve the interests of a debtor and creditors where the debtor is ‘capable of overcoming a current liquidity crisis if he is allowed a suitable space of time, or a certain amount of additional credit’.⁴²³ They are therefore intended to prevent the greater tragedy of bankruptcy. Although these arrangements are less costly than formal procedures and thereby conserve the debtor’s assets for the benefit of all, they pose significant risk to creditors and are inherently ‘unstable’ as creditors, irrespective of whether they participate in the arrangements or not, retain their rights to exercise all their legal remedies.⁴²⁴

Another informal route for resolving financial problems is the common law composition which Fletcher describes as ‘[s]omewhat more stable’ and as ‘a multi-party contract governed by common law’.⁴²⁵ Once again, such agreements may prevent bankruptcy, but creditors are vulnerable as a debtor may convince creditors to accept less than what the debtor can actually pay and an investigation into the debtor’s affairs, as is the case in the bankruptcy procedure⁴²⁶ and to some extent the voluntary arrangement procedure,⁴²⁷ is not conducted.⁴²⁸ Furthermore, non-

⁴²⁰ Fletcher *The law of insolvency* 45.

⁴²¹ *Idem* 85.

⁴²² *Idem* 45 and 85.

⁴²³ *Idem* 85.

⁴²⁴ *Ibid.*

⁴²⁵ *Ibid.*

⁴²⁶ See par 7.3.

⁴²⁷ See par 7.4.1.

⁴²⁸ Fletcher *The law of insolvency* 85.

participating creditors⁴²⁹ may continue with legal process against the debtor, thereby exposing his property.⁴³⁰

Commercial institutions developed the debt management plan⁴³¹ which credit providers regard as a debt collection method.⁴³² It entails a collective payment scheme that is customised to the debtor's income. Interest is generally suspended at the implementation of the plan that commonly does not provide for a discharge of debt. Commercial firms charge both set-up and management fees which Huls finds expensive.⁴³³ He also questions whether such institutions genuinely honour the debtor's interests as the most important. However, Huls also refers to alternative charitable 'free-to-client' firms operating under the consumer credit counselling services.⁴³⁴ These charities function on the basis that creditors pay a voluntary fee (deductible for taxation purposes) once the plan is successfully completed. As these are non-profit organisations the debtor's interests are prioritised. In this regard all possible options are considered and the one best suited to the client's needs (including bankruptcy) is chosen. Huls notes significant cost savings by the CCCS through substituting face-to-face consultancy with call centres and the internet.⁴³⁵ He concludes that market forces and technological innovation are the key drivers and that the English experience shows that there is a market for debt relief assistance and that creditors are willing to pay for it. However, it is limited as secured credit is excluded.⁴³⁶

7.6 Conclusion

The investigation into the natural person insolvency system in England and Wales was spurred by its reformist nature,⁴³⁷ the fact that it provides customised

⁴²⁹ Where participating creditors begin or continue legal process against the debtor it will result in fraud against the other creditors; Fletcher *The law of insolvency* 86.

⁴³⁰ *Idem* 86.

⁴³¹ See Huls 2012 *J Consum Policy* 504–505 for a discussion of this instrument.

⁴³² Ramsay 2012 *J Consum Policy* 430.

⁴³³ Huls 2012 *J Consum Policy* 504.

⁴³⁴ Hereafter 'CCCS'.

⁴³⁵ Huls 2012 *J Consum Policy* 504.

⁴³⁶ *Idem* 505.

⁴³⁷ Par 7.2.

procedures for different insolvency situations,⁴³⁸ its attribute of debtors' choice⁴³⁹ and that it was able to develop to its contemporary state from the position where South African insolvency law finds itself at present.⁴⁴⁰

The system provides for bankruptcy and three diverse formal statutory alternative debt relief procedures, in the form of IVAs, DROs and the CCAOs, and, unlike the South African system,⁴⁴¹ apparently caters for most insolvency situations in a satisfactory manner. The jurisdiction's philosophical foundations also include compassion for the debtor, unlike the South African direct and indirect unbalanced focus on advantage for creditors.⁴⁴² In fact, the CCAO procedure has fallen into disuse as debtors increasingly find recourse in other alternative statutory procedures.⁴⁴³ The CCAO procedure was therefore only considered in this chapter for completeness sake. Also contrary to the South African state of affairs, the system in England and Wales, in line with international principles and guidelines, focuses on debtor rehabilitation.⁴⁴⁴ Further in compliance with international principles and guidelines⁴⁴⁵ and contrary to the South African situation where all statutory debt relief procedures involve the overburdened courts,⁴⁴⁶ debtors' bankruptcy petitions will in future not be reliant on the courts.⁴⁴⁷ Also the DRO procedure and one route to an IVA are mostly administrative in nature.⁴⁴⁸

Depending on the elements of a particular case, more than one procedure may be applicable to a specific scenario and the debtor has a choice as regards his preferred measure. However, even though debtors generally decide as to the procedure most suited to their needs, the Insolvency Act pays mindful attention to the interplay between the procedures and thereby also guides the relevant

⁴³⁸ Para 7.3 and 7.4.

⁴³⁹ Par 7.1 and para 7.2–7.5 in general.

⁴⁴⁰ See par 7.2 and para 7.2–7.5 in general. See chs 3 and 4 as regards the South African situation.

⁴⁴¹ See chs 3 and 4.

⁴⁴² See ch 1 par 1.1, ch 3 par 3.3 and ch 4 in general as regards the South African focus.

⁴⁴³ Spooner *Personal insolvency law* 90 n655. See also McKenzie Skene and Walters 2006 *Am Bankr LJ* 497.

⁴⁴⁴ Fletcher *The law of insolvency* 43 read together with ch 2 par 2.7.

⁴⁴⁵ Ch 2 par 2.7.

⁴⁴⁶ Ch 3 par 3.3 and ch 4 para 4.2 and 4.3.

⁴⁴⁷ See s 71, sch 18 Enterprise and Regulatory Reform Act.

⁴⁴⁸ Ch 3 par 3.3 and ch 4 para 4.2 and 4.3.

institutions as to the most appropriate measure.⁴⁴⁹ Nevertheless, the system has been described as complex and confusing and still lacks proper coordination with individuals sometimes finding it difficult to make an informed choice.⁴⁵⁰ The system illustrates the need for impartial advice by intermediaries as regards the most suited measure where many options are available and where the choice rests with the debtor. As is the case in England and Wales, South African debtors theoretically have a choice between different statutory procedures in the sense that there is no objective third party that from the outset decides on the procedure most suited to the circumstances. However, South African legislation is lacking as regards the interplay between different procedures.⁴⁵¹ In this regard it has to be noted that the World Bank seemingly prefers the situation where a disinterested public agency from the outset makes the decision as to the best option available.⁴⁵² It is interesting that debt relief measures in England and Wales have not been consolidated in a single piece of legislation as the CCAO procedure forms part of the County Court Administration Act. However, the primary piece of legislation as regards debt relief, namely the Insolvency Act, has reformed to such an extent that the CCAO procedure is now redundant.⁴⁵³ South Africa may possibly draw from the experience in England and Wales by expanding procedures contained in the Insolvency Act rather than attempting to reform procedures forming part of legislation that are technically not mandated to deal with insolvency as such.

Turning to the specific procedures, the first procedure discussed is bankruptcy which may be compared to the South African sequestration procedure.⁴⁵⁴ However, unlike the South African state of affairs⁴⁵⁵ the law of England and Wales provides for relatively easy access as inability to pay poses the only substantive requirement as regards debtors' petitions. Also, the measure is primarily intended as a debt relief tool and is 'process friendly'.⁴⁵⁶ Nevertheless debtors face a considerable financial

⁴⁴⁹ See ss 251, 251K(4), 251M(7), 273(1), 274A, 276 and sch 4ZA(2)–(4).

⁴⁵⁰ See Walters 2009 *Int Insolv Rev* 12, McKenzie Skene and Walters 2006 *Am Bankr LJ* 496–497 and Ramsay 2012 *J Consum Policy* 430.

⁴⁵¹ See ch 3 par 3.3.2.3 and ch 4 para 4.2.5 and 4.3.4.

⁴⁵² *WB Report* 67.

⁴⁵³ Spooner *Personal insolvency law* 90 n655 and Spooner 2013 *ERPL* 756 n53.

⁴⁵⁴ Par 7.3 read together with ch 3 par 3.3.

⁴⁵⁵ Ch 3 par 3.3.2.

⁴⁵⁶ Walters and Smith 2010 *Int Insolv Rev* 192.

obstacle as a deposit and fees amounting to approximately £700 are required.⁴⁵⁷ This is, contrary to what is internationally accepted,⁴⁵⁸ because government does not consider bankruptcies as a 'public good' and therefore the 'user pay model' finds application.⁴⁵⁹ However, debtors not able to pay the bankruptcy fees may, unlike the South African situation, find recourse in alternative measures.⁴⁶⁰ As is the case in South Africa,⁴⁶¹ creditor petitions are allowed in England and Wales, although the procedure in terms thereof has, in line with international principles and guidelines,⁴⁶² been modernised by doing away with acts of bankruptcy. These were substituted with a tool termed 'statutory demand' which rather focuses on inability to pay and which has greatly simplified this area of law.⁴⁶³ It seems that South Africa is following this trend as a similar instrument has been introduced in the Insolvency Bill.⁴⁶⁴ In England and Wales and in order to curb abuse,⁴⁶⁵ a creditor petition may only be withdrawn with the permission of the court.⁴⁶⁶ The procedure also includes some provisions intended to limit debtors' abuse of process.⁴⁶⁷ Although the courts do consider whether the estate contains sufficient assets to prevent waste of energy and money⁴⁶⁸ before making a bankruptcy order, such indirect requirement is not solely focused on the interest of creditors, unlike the focus of its South African counterpart.⁴⁶⁹ The system in England and Wales unfortunately does not provide for a moratorium on debt enforcement once an application is lodged⁴⁷⁰ which is contrary to international best practice.⁴⁷¹ Unlike the South African position, the full bankruptcy process is only followed in England and Wales if, amongst others, the estate holds sufficient assets to render it worthwhile.⁴⁷² Although the system does not exclude all property and shifts the obligation to claim assets of excess value to the insolvency

⁴⁵⁷ Spooner *Personal insolvency law* 91.

⁴⁵⁸ Ch 2 par 2.7.

⁴⁵⁹ Ramsay 2012 *J Consum Policy* 430.

⁴⁶⁰ Spooner 2012 *Am Bankr LJ* 250.

⁴⁶¹ Ch 3 par 3.3.

⁴⁶² Ch 2 par 2.7.

⁴⁶³ Par 7.3.2 and Fletcher *The law of insolvency* 134.

⁴⁶⁴ See the discussion in ch 3 par 3.3.2.1.

⁴⁶⁵ See ch 2 par 2.7.

⁴⁶⁶ S 266(2). See also r 6.32.

⁴⁶⁷ See s 264(1)(c) read together with s 276.

⁴⁶⁸ See par 7.3.2 and authorities cited there.

⁴⁶⁹ See ch 3 par 3.3.2.2.

⁴⁷⁰ S 285.

⁴⁷¹ Ch 2 par 2.7.

⁴⁷² Par 7.3.3.

representative,⁴⁷³ it has an advanced exemption regime. In this regard no monetary thresholds are placed on exempt assets although the representative may claim excess value which partly adheres to international principles and guidelines.⁴⁷⁴ The jurisdiction also provides for a vehicle exemption and the home at least receives some recognition. In line with the ‘can pay should pay’ principle, an income payment order⁴⁷⁵ or agreement is competent in instances where the bankrupt has distributable net income available.⁴⁷⁶ This feature is an important trade-off for the benefits that the liberal discharge offers and is also available in South African law, although it is rarely used in practice in South Africa.⁴⁷⁷ The exemption regime in England and Wales has achieved an acceptable balance between the rights of all stakeholders⁴⁷⁸ which is dissimilar to the South African experience which is tremendously conservative to the detriment of debtors.⁴⁷⁹ A pertinent feature of the system in England and Wales is that the majority of bankruptcies are processed by the public official receiver that is attached to the relevant court,⁴⁸⁰ although the users of the system largely bear the costs.⁴⁸¹ In South Africa, no government agency steps in where the estate does not reflect sufficient value to defray the costs of sequestration. In fact, one of the entry requirements of the sequestration procedure is that the estate holds sufficient value to cover all sequestration costs.⁴⁸² England and Wales also have a liberal discharge administration as a debtor is generally automatically discharged after a period of one year.⁴⁸³ In South Africa, an automatic discharge only takes place once the exorbitant period of ten years has lapsed.⁴⁸⁴ The brief period after which an automatic discharge takes place in England and Wales has been balanced by provisions providing for a court suspension of the procedure and new powers as regards post-discharge restrictions where the bankrupt’s conduct has been unsatisfactory.⁴⁸⁵ This coincides with the international principle that good behaviour may be set as a

⁴⁷³ Ch 2 par 2.7.

⁴⁷⁴ *Ibid.*

⁴⁷⁵ S 310.

⁴⁷⁶ S 310A.

⁴⁷⁷ See s 23(5) of the South African Insolvency Act 24 of 1936 and ch 3 par 3.3.2.2.

⁴⁷⁸ Evans *A critical analysis* 132–133.

⁴⁷⁹ See ch 3 par 3.3.3.

⁴⁸⁰ Ramsay 2006 *U III L Rev* 252 and 271, Walters 2009 *Int Insolv Rev* 16 and Ramsay 2012 *J Consum Policy* 428.

⁴⁸¹ Walters 2009 *Int Insolv Rev* 17.

⁴⁸² Ch 3 par 3.3.2.1.

⁴⁸³ S 279(1).

⁴⁸⁴ See ch 3 par 3.3.4.

⁴⁸⁵ Fletcher *The law of insolvency* 362. See ss 279(3) and 281A.

condition for the discharge⁴⁸⁶ and is very attractive when contemplating a possible trade-off for recommending a reduced period after which the South African sequestration period automatically comes to an end. However, the short period after which a discharge is granted in England and Wales raises concerns as debtors making use of an alternative procedure (to bankruptcy) may not receive the same preferential treatment. Furthermore, those responsible for the protection of the public interests are placed under considerable pressure to assess the bankrupt's pre-bankruptcy conduct within such a short period of time.⁴⁸⁷ The present dispensation may also lead to a progressive loss of prudent social attitudes.⁴⁸⁸ As regards the effect of the discharge, it releases the bankrupt from all bankruptcy debts⁴⁸⁹ and is generous as such debts are broadly defined and non-dischargeable debts are restricted.⁴⁹⁰ The discharge also generally lifts all legal restraints and disqualifications relating to the bankrupt.⁴⁹¹ The broad discharge and its liberating effects are in line with international principles and guidelines.⁴⁹² McKenzie Skene and Walters note that bankruptcy may be a logical choice for consumers with limited non-exempt assets and little surplus income and for those with few assets but who possess surplus income as income payment orders in bankruptcy cannot stretch beyond three years where IVAs generally run for five years.⁴⁹³

The IVA procedure⁴⁹⁴ is the first of three alternatives to bankruptcy that could in some respects be compared with the South African statutory composition⁴⁹⁵ and proposed pre-liquidation composition⁴⁹⁶ procedures as it constitutes an arrangement with creditors. The plan may be forced upon passive and dissenting creditors where the required majority vote is obtained, but other than that a repayment plan cannot be ordered by a disinterested party. Apart from the possibility of obtaining a section 310 income payment order in bankruptcy procedures, the procedure basically

⁴⁸⁶ Ch 2 par 2.7.

⁴⁸⁷ *Idem* 363.

⁴⁸⁸ *Idem* 364.

⁴⁸⁹ S 281(1).

⁴⁹⁰ McKenzie Skene and Walters 2006 *Am Bankr LJ* 482.

⁴⁹¹ See Fletcher *The law of insolvency* 370–372.

⁴⁹² Ch 2 par 2.7.

⁴⁹³ McKenzie Skene and Walters 2006 *Am Bankr LJ* 484.

⁴⁹⁴ See par 7.4.1.

⁴⁹⁵ See ch 3 par 3.4.

⁴⁹⁶ See ch 5 par 5.2.

represents the most prevalent statutory payment plan (or rehabilitation) procedure in England and Wales and it is therefore odd that courts (or administrative bodies) cannot intervene by forcing plans on parties. However, the liberal and generally open access bankruptcy dispensation may be a significant motivation for creditors rather to reach an agreement with debtors than lose more through bankruptcy. The proposal may involve assets, income or both. The procedure is regularly used to avert the sale of a home in bankruptcy proceedings⁴⁹⁷ and in such instances salaried homeowners are generally expected to release some equity and to make income contributions. The measure is also used to circumvent bankruptcy and its restrictions, but is also competent once bankruptcy has been applied for and even after such an order was granted. When the procedure is measured against international principles and guidelines it must firstly be kept in mind that the most recent international report, namely that of the World Bank, regards the benefits of voluntary procedures as mostly illusionary.⁴⁹⁸ However, certain elements do have the potential to enhance the probability of its success.⁴⁹⁹ Of these, the IVA procedure includes a cram down where a majority vote is obtained as well as the feature that passive creditors should not be able to hinder agreements.⁵⁰⁰ The introduction of section 256A reduces the total costs of the procedure under certain circumstances which is in line with the principle that costs should not pose an obstacle to resolving financial problems through an informal route. However, the procedure does not specifically provide for legal aid or debt counselling services and a moratorium on debt enforcement does not become effective once the process is set in motion.⁵⁰¹ As the IVA procedure is voluntary in nature it cannot be compared to the South African repayment plan procedures⁵⁰² and has little to offer to researchers contemplating the possible reform of such procedures. Nevertheless, it seems that in practice the measure is functioning well due to it being routinised and as industry has agreed to standardised norms.⁵⁰³

⁴⁹⁷ Steyn 2012 *De Jure* 641–642.

⁴⁹⁸ *WB Report* 46. See ch 2 para 2.6.2.1 and 2.7.

⁴⁹⁹ See ch 2 par 2.7.

⁵⁰⁰ *Ibid.*

⁵⁰¹ *Ibid.*

⁵⁰² See ch 4 par 4.2 as regards the administration order procedure and par 4.3 relating to the debt review procedure.

⁵⁰³ Par 7.4.1.

The DRO procedure⁵⁰⁴ was introduced in England and Wales specifically to provide for NINA cases, not because these debtors were formally excluded from all of the statutory procedures that existed before the measure was implemented but because they were not feasible in NINA circumstances.⁵⁰⁵ As regards bankruptcy specifically, NINA debtors are not able to pay the fees thereof and government is adamant that the bankruptcy procedure should remain self-financing. In South Africa, NINA debtors do not have access to any statutory procedure due to unconcealed substantial requirements which have resulted in an unattainable unconstitutional dispensation.⁵⁰⁶ It is heartening to find studies which report preliminary evidence of the effectiveness of the DRO procedure in England and Wales and its ‘significant impact on the wellbeing of debtors’. However, these studies record overwhelming support for an increase in the maximum debt threshold and assets that a debtor may possess when applying for a DRO.⁵⁰⁷ The DRO procedure is mostly compliant with international principles and guidelines as it is not generally reliant on courts, disregards secured debt, does not provide for creditor participation as a matter of course and allows for a wide discharge. However, in contrast with international principles and guidelines, the moratorium on debt enforcement only becomes effective once the order is made.⁵⁰⁸ As regards the discharge, the one-year period is particularly short, although the possibility of a debt relief restriction order does countervail moral hazard. Nevertheless, in modern law the period for which insolvency proceedings are effective also serves important educational purposes and therefore the one-year period seems unbalanced. Another consideration relates to equality. In England and Wales the IVA procedure will generally run for a period of five years which is disproportionate to the one-year period in DRO (and also bankruptcy) proceedings.⁵⁰⁹

The English and Welsh natural person insolvency system’s continuous evolution in response to modern needs is noteworthy. In particular, the Tribunals, Courts and

⁵⁰⁴ Par 7.4.2.

⁵⁰⁵ Department for Constitutional Affairs *A choice of paths* 16–17 <http://bit.ly/1TXAQAA> (accessed 21 August 2015).

⁵⁰⁶ See ch 1 par 1.1, ch 3 par 3.5 and ch 4 par 4.4.

⁵⁰⁷ Department for Business Innovation and Skills *Insolvency proceedings 2* <http://bit.ly/1PDfD9c> (accessed 21 August 2015).

⁵⁰⁸ Par 7.4.2 read together with ch 2 par 2.7.

⁵⁰⁹ Ch 2 par 2.7.

Enforcement Act's policy (that does not favour entirely unrestricted access to the bankruptcy discharge, but that rather expands access to repayment plans as the preferred consumer alternative with a NINA measure for the poor)⁵¹⁰ creates a healthy balance between the different contemporary market interests. The system's progression towards administrative rather than judicial proceedings is also commendable especially in light of the latest reforms that will render debtors' bankruptcy petitions administrative in nature.⁵¹¹ Another attractive element of the system as a whole is that those who are able to afford a particular measure bears the costs of its administration, but only a minimal fee is charged to those who make use of the DRO procedure which is also streamlined to keep costs to a minimum. Therefore, the costs restricting access to for instance the bankruptcy procedure may be justified as sufficient alternative measures exist. Other refreshing features in line with international principles are the possibility of restriction orders (that have substituted previous stigmatising restrictions, prohibitions and disqualifications that applied automatically to all bankrupts) in both the bankruptcy and the DRO procedure which ensure that dishonest and culpable debtors are penalised as the public needs protection against this minority of debtors.

⁵¹⁰ Ramsay 2012 *J Consum Policy* 426–427.

⁵¹¹ See s 71, sch 18 of the Enterprise and Regulatory Reform Act which inserted the new administrative procedure contained in ss 263H–O into the Insolvency Act.

CHAPTER 8: CONCLUSION

SUMMARY

8.1 Principal objectives and general conclusions

8.2 Recommendations for law reform

8.3 Concluding remarks

8.1 Objectives and general conclusions

The overreaching research objectives of this thesis were to re-evaluate the adequacy of the current South African natural person insolvency system as a response to modern-day needs and to point out the way forward.¹ The problem relates not only to access to debt relief but also to the efficiency of existing debt relief measures viewed both individually and holistically, in providing the diverse scope of financially overcommitted South African debtors with a viable prospect of a new start.² The South African natural person debt relief system was compared with and evaluated against contemporary international developments, principles and guidelines. Comparative studies with the natural person insolvency systems of New Zealand³ and England and Wales⁴ were undertaken to draw inferences on whether any of these systems' attributes could be considered for law reform in South Africa. The ultimate aim of the study is to make suggestions for law reform which this chapter sets out to do.

From the preliminary outline of the South African measures in chapter one it was already clear that the current system does not provide adequate access from a debt relief perspective and that it is generally non-responsive to modern-day socio-economic needs.⁵ In addition, the majority of insolvent natural person debtors and more specifically the no income and no assets group (NINA debtors which concept

¹ See ch 1 par 1.2.

² *Ibid.*

³ See ch 6.

⁴ See ch 7.

⁵ Ch 1 par 1.1.

does not only refer to literally no income and no assets, but also to insufficient attachable assets and income to contribute towards debt) is totally excluded from access to the system. The marginalisation of specifically NINA debtors is tragic due to the socio-economic conditions that South Africans are faced with today. As pointed out above⁶ the country is riddled with exorbitant unemployment rates, very many households that are reliant on social grants and, in contrast, a very low percentage of the population who are liable for individual tax. Adding insult to injury, South Africans are arguably the most indebted individuals in the world. Although efficient and effective natural person insolvency measures will not provide a cure to these ailments, the exclusivity of the broader insolvency regime further perpetuates the situation by supporting the duality of the South African economy. This is because it retains some South African debtors in a state of perpetual poverty or forces some forming part of the formal economy to enter the secondary economy which may result in them becoming NINA debtors. It is thus clear that the system is not accustomed to the contemporary South African socio-economic environment. In other terms, financially over-committed South Africans are in need of incentives to become economically productive citizens and in this respect I am of the opinion that access to an efficient and effective insolvency system can make a valuable contribution.⁷

As regards the current state of the natural person insolvency system, it is clear from the discussions in previous chapters that when the system as a whole is evaluated from a constitutional perspective, it fails miserably in terms of the right to equality. This is so as it unjustifiably and unreasonably discriminates against debtors not only by refusing access to the NINA group (on the basis of financial grounds) but also as some of those who are fortunate enough to qualify for entry to the administration and debt review procedures may, due to the absence of a discharge, be subjected to those procedures for unconscionable payment periods in comparison with debtors who qualify for the sequestration procedure specifically and who are generally eligible for a discharge after a period of four years.⁸ It flows from discussions above⁹

⁶ *Ibid.*

⁷ *Ibid.*

⁸ See ch 1 par 1.1, ch 3 par 3.5 and ch 4 par 4.4.

⁹ *Ibid.*

that, as all natural person insolvents are by definition factually unable to service their debt and in some instances face comparable socio-economic adversities as a result thereof, they should be similarly treated. What would in my view constitute equal treatment is that all honest but unfortunate debtors should have access to a debt relief procedure and that every measure should lead to the same end result, namely, a discharge of debt.¹⁰

From the discussions above it is apparent that the main issue as regards access is the sequestration procedure's advantage for creditors requirement that stands in the way of debtors accessing the fresh start that only that procedure offers.¹¹ This requirement stems from the fact that the procedure is only indirectly regarded as a debt relief measure, due to its object of regulating the sequestration process to ensure an orderly and fair distribution of assets to the advantage of creditors.¹² Furthermore, it is a costly procedure to employ and it would therefore not make sense to apply its features to estates of trivial value.¹³ Many debtors, mostly those forming part of the NINA category are, because of entry requirements and specifically the necessity of distributable income, not only excluded from the sequestration procedure, but also from accessing secondary measures which mostly represent repayment plans.¹⁴ Furthermore, even where debtors do gain entry to these secondary measures, namely, the administration and debt review procedures, they will only truly assist mildly over-indebted individuals as neither procedure leads to a discharge of debt. This is despite the fact that these measures were (quite ironically and in contrast with the sequestration procedure) drafted for the primary benefit of debtors.¹⁵ Consequently, while existing secondary procedures are useful in instances where debtors are in need of temporary respite they do not offer real relief to heavily over-indebted individuals, firstly as such debtors do not necessarily meet the access criteria, and secondly as the twin features of repayment plans, namely, a discharge and maximum payment period, are not provided for.¹⁶ In fact, in many

¹⁰ See ch 3 par 3.5 and ch 4 par 4.4.

¹¹ Ch 3 par 3.6.

¹² *Ibid.*

¹³ *Ibid.*

¹⁴ *Ibid.*

¹⁵ *Ibid.*

¹⁶ Ch 4 par 4.5.

instances the application of the secondary procedures only perpetuates insolvent circumstances.¹⁷ On another level, it has been found that the sequestration procedure's advantage for creditors requirement, which serves an important government purpose, can only be saved from unconstitutionality if proper alternative measures leading to a discharge are available to debtors who are excluded from its ambit¹⁸ – which is evidently not the case at present.¹⁹

Apart from access and the most important aspect regarding the efficiency of debt relief procedures, namely the discharge, it was seen that the system is further plagued by various inadequacies. These mostly stem from the fact that the system as a whole is devoid of proper unified policy directives.²⁰ This deficiency can be attributed to the fact that more than one government department are involved,²¹ that the current debt relief measures have developed in a haphazard fashion²² and that no holistic review of the system was ever undertaken. This incoherency has led to further intricacies as different pieces of legislation and multiple regulators, intermediaries and decision-making forums are involved.²³ Also, the interplay between the different pieces of legislation and procedures has not received much attention.²⁴ The latter failure in turn left debtors, who must make the decision as to the procedure most suited to their circumstances (as opposed to independent government agencies fulfilling the function) at almost impossible crossroads – which has contributed to much unnecessary litigation in the field.²⁵

As regards the most pertinent reform process in the area at the moment, namely the proposed Insolvency Bill, the Law Reform Commission has made sensible proposals relating to the sequestration procedure specifically. However, the commission and consequently the reform is not focused on debt relief and therefore the reform proposals fail to suggest a holistic solution to the problems associated with the

¹⁷ *Ibid.*

¹⁸ See ch 3 para 3.5 and 3.6.

¹⁹ Ch 4 par 4.5.

²⁰ See ch 4 para 4.2.7 and 4.3.6.

²¹ Ch 1 par 1.1.

²² See ch 3 para 3.2 and 3.3.1 and ch 4 para 4.2.1 and 4.3.2.

²³ See ch 3 par 3.3 and ch 4 par 4.2 and 4.3.

²⁴ Ch 3 par 3.3.2.3 and ch 4 par 4.3.4.

²⁵ *Ibid.*

broader natural person insolvency law at present.²⁶ Another major shortcoming in this respect is that the debt review and administration order procedures do not form part of the reform. Although the commission's intention with the proposed pre-liquidation composition is to provide an opportunity for a fresh start to those who do not qualify for liquidation proceedings, it is apparent that the proposal in its current form will not reach this goal. This is mainly because the commission aims to force debtors who in most instances do not have any negotiating power to negotiate with creditors as a prerequisite for a discharge. Also, high costs are involved which will further exclude many debtors from utilising this procedure.²⁷

From the discussions of ancillary measures it was obvious that, save for court-ordered debt review in terms of section 85 of the National Credit Act,²⁸ these procedures do not increase access to the insolvency system as a whole.²⁹ As regards section 85 specifically, it does not have a drastic effect as regards access and does not provide access to or assist NINA debtors.³⁰ Further, the ancillary measures do not find application in every natural person insolvency case and consequently do not significantly contribute to the system's efficiency as a whole.³¹ Nevertheless, where they do find application they may be employed together with the primary and secondary debt relief procedures which could lead to improved relief.³²

From the above considerations it is clear that reform is necessary. In this respect guidance was sought in international principles and guidelines and comparative jurisdictions which lead to the recommendations below.

²⁶ Ch 3 par 3.3.

²⁷ Ch 5 par 5.9.

²⁸ 34 of 2005 (hereafter 'the NCA').

²⁹ Ch 5 par 5.9.

³⁰ See ch 5 para 5.2 and 5.9.

³¹ Ch 5 par 5.9.

³² *Ibid.*

8.2 Recommendations for law reform

8.2.1 General

In my re-evaluation of the South African insolvency system, universal solutions to South African insolvency-related problems, which are not unique, were considered and therefore the most significant international trends and guidelines were observed.³³ Some of the recommendations in this chapter are based on the latter. Where good reasons exist for deviation from strong preferences it is explained. However, before turning to more specific aspects, the three fundamental assumptions that were reduced from the discussions of international trends and guidelines in chapter two and which are accepted in this thesis are repeated. These are that³⁴

- a. an effective natural person insolvency system is essential in modern credit-driven economies;
- b. although the introduction of or developments in natural person insolvency systems may pose concerns along the lines of debtors' moral hazard, fraud and stigma, the many benefits of an advanced system prevail over such concerns, which can be overcome; and
- c. a balance between the rights of debtors, creditors and society (the three beneficiaries of effective distressed debt regulation) should be maintained.

The three most salient themes of the World Bank *Report* are also generally endorsed. These are that³⁵

- a. formal debt relief measures are needed to force a discharge of debt;
- b. negotiated workouts are not preferred although former reports favour such measures. This is as their benefits are mostly illusory and most often fail. In a developing country (such as South Africa) the optimal use of resources is paramount and therefore unnecessary and generally ineffective procedural layers should be avoided, irrespective of their theoretical appeal; and
- c. most importantly, some conditions for relief are set which coincide with the emphasis placed on the need for a balance between the rights of debtors and creditors.

³³ Ch 2.

³⁴ Ch 2 par 2.7.

³⁵ Ch 2 par 2.6.3.

The most pertinent international principles and guidelines relevant to this thesis were summarised in chapter two³⁶ which set a framework against which both the South African³⁷ and comparative systems, namely New Zealand³⁸ and England and Wales,³⁹ were measured. However, as was mentioned the ultimate aim was to draw from it in considering possible solutions to shortcomings in the South African system specifically. Conclusions and specific recommendations in this chapter will therefore be made and explained in light of the international principles (which overlap in many instances) that were extracted in chapter two – although not in the same sequence. These are:

- a. *Regulation and administration of an insolvency system.* This issue will receive attention first as it impacts on many of the discussions that follow.
- b. *Access to all honest but unfortunate debtors.* This principle is secondly dealt with as it also influences subsequent discussions.
- c. *Discharge.* Discharge is the most pertinent principle and receives special attention as it forms the centre of many of the later discussions.
- d. *Multiple procedures depending on the debtor's circumstances.* I prefer multiple procedures and the discussion of these take up the larger part of this chapter, as this is where the different elements of a functioning system meet. I am in favour of four procedures, namely, a liquidation procedure, a repayment plan (rehabilitation) procedure, a free-standing NINA procedure and a voluntary negotiated procedure.
- e. *Financing issues.* The manner in which the system should be financed is discussed after the different procedures have been examined.
- f. *Non-discrimination.* Non-discrimination is the last principle that receives specific attention although it constitutes an on-going theme throughout discussions in this chapter. In this respect recommendations are formulated that relate to non-discrimination as regards entry to debt relief procedures whilst the debtor is subject to any insolvency procedure and the discharge.

³⁶ Ch 2 par 2.7.

³⁷ See chs 3 and 4 in general.

³⁸ Ch 6.

³⁹ Ch 7.

Although the above-mentioned international principles set out the structure for recommendations and signify important uniform goals for reform, recommendations in this chapter also draw strongly from positive attributes of the comparative jurisdictions, namely New Zealand⁴⁰ and England and Wales.⁴¹

Over and above recommendations structured in terms of the principles elevated above, the paragraph is concluded with recommendations relating to ancillary debt relief measures. Concluding remarks follow which draw this chapter and consequently also this thesis to a close.

8.2.2 Regulation and administration

Although aspects relating to regulation and administration will also be dealt with when the proposed different measures are discussed below,⁴² overarching recommendations having a collective effect on many of the further considerations in this respect need to be offered from the onset. The first relates to the best suited government department to oversee natural person insolvency. At present two departments, namely the Department of Justice⁴³ and the Department of Trade and Industry⁴⁴ are involved in the field. As was mentioned, this division has contributed to the fragmented and unprincipled manner in which this area of the law has developed.⁴⁵ I recommend that the Department of Trade and Industry should fulfil this role. This is because the department is responsible for the regulation of the credit industry which logically includes distressed credit – the main reason for natural person insolvency. Furthermore, the department's responsibility to strengthen the economy coincides with the internationally regarded central object of natural person insolvency law, namely the economic rehabilitation of debtors.⁴⁶ In New Zealand⁴⁷ and England and Wales⁴⁸ natural person insolvency correspondingly resorts under

⁴⁰ Ch 6.

⁴¹ Ch 7.

⁴² Par 8.2.5.

⁴³ See ch 3 par 3.3 as regards the sequestration procedure and ch 4 par 4.2 relating to the administration order procedure.

⁴⁴ See ch 4 par 4.2 relating to the debt review procedure.

⁴⁵ Par 8.1.

⁴⁶ See ch 2 par 2.7. See also par 8.2.4.1.

⁴⁷ See ch 6 par 6.2.

⁴⁸ See ch 7 par 7.1.

the Ministry of Business, Innovation and Employment and the Department of Trade and Industry respectively.

I also recommend that, as was gathered from the unique French system, the South African Reserve Bank (who is eager to assist large financially failing credit providers)⁴⁹ should be consulted in the reform process. This is as its participation would, amongst others, enhance the credibility of the reforms – especially from the financial and more specifically the banking sector’s perspective.⁵⁰ However, I do not suggest that the bank should in any way become involved in the physical administration of debt relief procedures (as is the case in France)⁵¹ – only that its expertise and partaking in reform would be beneficial.

In consonance with my recommendation as regards the most suited government department, insolvency legislation should resort under the Department of Trade and Industry. As regards the different pieces of legislation I recommend that all natural person insolvency procedures should resort under the Insolvency Act⁵² as is the case in New Zealand⁵³ and mostly in England and Wales.⁵⁴ This suggestion will contribute to a simpler, more streamlined and coherent system. For the same reasons, I recommend that the reform of all natural person insolvency procedures should take place simultaneously, as was done in the most recent reform process in New Zealand.⁵⁵ Such comprehensive reform should transpire within the confines of clear policy objectives and in this respect I recommend that the South African reform should, like the New Zealand reform,⁵⁶ be structured around the following:

- a. Economic rehabilitation of insolvent debtors: This should be the main aim of insolvency law and would benefit debtors, creditors and society at large.
- b. Modernisation: In this respect international principles and guidelines should be considered.

⁴⁹ See ch 1 par 1.1.

⁵⁰ See ch 2 par 2.4.

⁵¹ *Ibid.*

⁵² 24 of 1936.

⁵³ See ch 6 par 6.1.

⁵⁴ See ch 7 par 7.1.

⁵⁵ See ch 6 par 6.2.

⁵⁶ *Ibid.*

- c. The improvement of processes: General alignment with civil procedure and specifically individual enforcement procedures is important. Further, the interplay between different statutory measures should receive conspicuous attention.
- d. Simplicity and efficiency: In a developing country these two attributes should score high in any reform initiative.
- e. Proceeds distribution that is mostly consistent with individual enforcement proceedings: The protection of secured creditors' rights in all procedures will go a long way in procuring buy-in from industry and would greatly simplify the system. This policy consideration overlaps with the improvement of processes.
- f. Maximising creditor returns: The 'earned fresh start' policy⁵⁷ should be followed where it is expected from debtors to do the best that they can for a restricted period of time to be rewarded with a discharge at the end thereof.

As regards specific objectives of the Act itself I recommend that a purpose statement be included where the economic rehabilitation of the debtor is highlighted as the main objective of the Act. Focusing on debtor rehabilitation would benefit all involved as is apparent from international principles and guidelines.⁵⁸ This principal goal is also followed in New Zealand⁵⁹ and England and Wales.⁶⁰ However, it should further be explicitly stated that, within the Act's broader object of debtor rehabilitation, it strives to balance the rights of the debtor, creditors and society at large.⁶¹

Another matter relating to regulation and administration is the degree to which natural person insolvency procedures should be reliant on the judiciary. In this respect international guidelines suggest that courts will always have a role to play, as insolvency law regulates the rights of creditors and debtors (in insolvent circumstances) which are ultimately adjudicated and enforced by the judiciary. Also, recourse to the courts is a human rights issue. However, court involvement should be the exception rather than the rule, as in instances where a debtor seeks debt relief through formal involuntary insolvency procedures, a need for a practical rather than a legal solution is sought. Therefore, court functions should be counterbalanced

⁵⁷ See par 8.2.1.

⁵⁸ See ch 2 par 2.7.

⁵⁹ See ch 6 para 6.1 and 6.2.

⁶⁰ See ch 7 para 7.1 and 7.2.

⁶¹ See par 8.2.1.

by strengthening public administrative bodies. In this respect, developing countries should consider the context of existing institutions and infrastructures.⁶² Although the involvement of the judiciary in comparative jurisdictions, namely New Zealand⁶³ and England and Wales,⁶⁴ are further referred to below,⁶⁵ it is notable that both have migrated to a mostly extra-judicial system. In line with the above, I recommended that a strong public institution should take over some of the functions that South African courts traditionally fulfil and that existing infrastructure should be considered in this regard. In this respect South Africa can draw from the French system that tasked its central bank with the administration of the insolvency system.⁶⁶ I submit that the National Credit Regulator,⁶⁷ which already resorts under the Department of Trade and Industry, is the best suited South African institution to deal with these matters. However, I propose that the master of the high court should remain involved in the sequestration procedure.⁶⁸ I recommend that the NCR's functions be expanded to include:

- a. the registration and regulation of all insolvency practitioners in the wide sense of the word;
- b. debtor education on the different insolvency measures available;
- c. debtor advice as to the procedure most suited to individual needs; and
- d. overseeing the proposed repayment plan procedure and the administration of the proposed NINA procedure.⁶⁹

As regards the regulation of intermediaries, all insolvency practitioners should be registered with and regulated by the NCR. As the NCR is already tasked with similar duties as regards the debt review procedure, it can develop and expand on its existing functions. A balance should be attained between ensuring that intermediaries are qualified to address the problems of insolvents and prohibiting undue restriction on intermediaries who may offer advice and assistance.⁷⁰ Although

⁶² See ch 2 para 2.6.2.1; 2.6.2.2 and 2.7.

⁶³ See ch 6 par 6.7.

⁶⁴ See ch 7 par 7.6.

⁶⁵ See par 8.2.5.

⁶⁶ See ch 2 para 2.4 and 2.7.

⁶⁷ Hereafter the 'NCR'.

⁶⁸ See par 8.2.5.2.

⁶⁹ The latter proposed functions are further explained in para 8.2.5.3 and 8.2.5.4.

⁷⁰ Ch 2 par 2.6.2.2.

intermediaries need not be from the same generic profession, I recommend that they should belong to a profession accredited by the minister. However, this does not mean that all accredited and registered practitioners should be able to act as intermediaries in all procedures as the minister needs to ensure that the level of skill is aligned with the needs of a particular procedure. Therefore, practitioners from different professions could be assigned different procedures. If this model is followed, vested interests could be taken into consideration whilst the regulation of intermediaries, that is for instance a problem in the administration order procedure at present,⁷¹ is improved. Also, the NCR could introduce measures to ensure that debtors receive quality advice across the spectrum. This is especially needed in a multi-track system where intermediaries may further their own financial or ideological interests. A final word as regards insolvency practitioners is that the Insolvency Act should provide clear recourse where practitioners do not adhere to the Act or are lax in fulfilling their duties.

8.2.3 Access to all honest but unfortunate debtors

It was pointed out above that the South African natural person insolvency system's exclusion of some honest but unfortunate debtors results in socio-economic ills⁷² and is unconstitutional.⁷³ Also, all international insolvency reports call for the inclusion of all such debtors.⁷⁴ I consequently recommend that all honest but unfortunate South African debtors should have access to the natural person insolvency system. In this respect the legislature should not only attend to formal access, but also substantive access as cost should not pose an obstacle.⁷⁵ This is further dealt with in the recommendations relating to the different alternative measures below.⁷⁶

Also, I recommend that the legislature make use of clear objective access rules as regards the different procedures and that the responsibility should not be passed to a gate-keeper (the courts and the NCR) by means of subjective standards.⁷⁷ In this

⁷¹ See ch 4 par 4.2.4.

⁷² Ch 1 par 1.1.

⁷³ See ch 4 par 4.4.

⁷⁴ See ch 2 par 2.7.

⁷⁵ *Ibid.*

⁷⁶ Par 8.2.5.

⁷⁷ See ch 2 par 2.6.2.3.

regard, I have one reservation which relates to the asset liquidation procedure which is further explained below.⁷⁸

It is recommended that access should only be restricted in cases of fraud or serious misconduct,⁷⁹ although I am not in favour of an inquest at the application stage of any debt relief procedure. This is because society only needs protection against a minority of unscrupulous debtors⁸⁰ and therefore a default inquest into debtors' good faith at the application stage would be excessive and therefore wasteful. In this respect I recommend that interested parties should rather, as is the case in New Zealand⁸¹ and England and Wales,⁸² be able to challenge the realisation of certain benefits to the debtor, for instance the discharge or to re-enter the credit-economy, at a later stage.⁸³

Another recommendation regarding access is that the internationally favoured liquidation test – focusing on the inability to pay debts – should be used as an entry standard in all procedures. This test should be based on the current inability to service present debts.⁸⁴

8.2.4 Discharge

8.2.4.1 Theoretical basis: economic rehabilitation

As was explained above with reference to international principles,⁸⁵ there are three theoretical justifications for the discharge, namely, the rehabilitation theme, the mercy theme and the collection theme.⁸⁶ The mercy theme is entrenched in morality and basic humanity and calls on the law to show compassion and mercy to honest but unfortunate debtors. The collection theme is based on the notion that a discharge motivates a debtor to collaborate with creditors to disclose property, avoid a multiplicity of collection procedures and provide for an equal distribution of value.

⁷⁸ Par 8.2.5.2.

⁷⁹ Ch 2 par 2.7.

⁸⁰ Ch 2 par 2.6.1.

⁸¹ See for instance ch 6 par 6.3.4.

⁸² See for instance ch 7 para 7.3.4 and 7.4.2.

⁸³ Ch 2 par 2.6.2.3.

⁸⁴ See ch 2 par 2.7.

⁸⁵ Ch 2 par 2.2.

⁸⁶ *Ibid.*

The rehabilitation theme entails that when a debtor is freed from his past responsibilities he will have a new incentive to engage in productive economic activity.⁸⁷ The collection theme has generally been discredited as insolvent natural person debtors have little to offer creditors.⁸⁸ Nevertheless, it is still relevant within the South African sequestration procedure with its direct advantage for creditors requirement⁸⁹ and also to some extent within the field of current repayment plans.⁹⁰ However, it does not provide a justification for a discharge in NINA circumstances where no collectable value exists. Although the mercy theme is discarded in the United States of America⁹¹ as a result of contemporary debt collection restrictions and the protection of debtors' personal liberty⁹² it is still relevant in South Africa as very few assets are excluded from individual enforcement measures.⁹³ As for the rehabilitation theme, it is extremely relevant within the South African socio-economic environment and specifically as regards NINA debtors who cannot, due to limited resources, use the organisation of business or other safety nets, for example insurance contracts, to shield them from financial risk.⁹⁴ Consequently, there are sufficient general theoretical justifications to provide all honest but unfortunate South African debtors with a discharge of excessive debt. Contributing to these justifications and even more important within the South African context is that the system's allowance of a discharge in some instances whilst excluding it in others, are in some instances unconstitutional.⁹⁵ I consequently recommend that all South African natural person debt relief measures should provide for a discharge of debt. Although the frontrunner as regards the discharge, namely the USA, has provided for a straight discharge or fresh start⁹⁶ it has of late also moved closer to the notion of an earned start as is favoured in Europe.⁹⁷ An 'earned new start' is also generally

⁸⁷

Ibid.

⁸⁸

Ibid.

⁸⁹

See ch 3 par 3.3.2.2.

⁹⁰

See ch 4 para 4.2.1 and 4.3.2.

⁹¹

Hereafter the 'USA' or 'American'. See ch 2 par 2.2.

⁹²

Ch 2 par 2.2.

⁹³

See ch 1 par 1.1.

⁹⁴

Ibid.

⁹⁵

Ch 1 par 1.1; ch 3 par 3.5 and par 4 par 4.4. See also par 8.1.

⁹⁶

Ch 2 par 2.2.

⁹⁷

See ch 2 par 2.3.

favoured by international principles and guidelines⁹⁸ and in New Zealand generally⁹⁹ as well as England and Wales.¹⁰⁰ In line with these trends and the importance of achieving a balance between the interests of debtors, creditors and society,¹⁰¹ I recommend that the South African discharge should be earned. What would be expected from debtors in a given scenario would become clearer from the recommendations below.¹⁰²

Apart from the discharge that embodies the first and most important element of economic rehabilitation, debtors should be competent to avoid excessive debt in future.¹⁰³ Although compulsory financial education and debt counselling (in the counselling sense of the word and not as a reference to the formal procedure in South African law)¹⁰⁴ seem attractive in reaching this goal, they necessitate significant resources whilst their efficiency is questioned.¹⁰⁵ In a developing country, resources should not be wasted on stints that would not result in concrete outcomes and therefore I do not support the idea of compulsory financial education and ‘debt counselling’ in the South African context. This is not to say that the outcomes that such endeavours wish to achieve are not important. In fact, if any concrete evidence as to the efficiency of such programs existed, it would have been necessary to raise funds for such initiatives. The goal of assisting the debtor to avoid insolvency in future as well as the last element as regards economic rehabilitation, namely non-discrimination after relief was granted¹⁰⁶ form part of subsequent discussions.¹⁰⁷

A last observation as regards the rehabilitation theme is that the debtor’s ability to retain excluded property improves the outcome of the discharge as debtors are

⁹⁸ Ch 2 par 2.7. See also 8.2.1.

⁹⁹ See ch 6 para 6.3, 6.4, 6.5.1 and 6.5.2. The no asset procedure apparently does not follow this approach; ch 6 par 6.5.3.

¹⁰⁰ See ch 7 par 7.2.

¹⁰¹ See also par 8.2.1.

¹⁰² Par 8.2.5.

¹⁰³ See ch 2 par 2.6.2.6.

¹⁰⁴ See ch 4 par 4.3.

¹⁰⁵ Ch 2 par 2.6.2.6.

¹⁰⁶ *Ibid.*

¹⁰⁷ Para 8.2.4.2, 8.2.4.3, 8.2.5.2, 8.2.5.3 and 8.2.5.4.

provided with the necessities to carry on with their lives.¹⁰⁸ This issue will receive further attention when the liquidation procedure is discussed.¹⁰⁹

8.2.4.2 Period and manner in which the discharge is achieved

I recommend that a generic automatic discharge after a period of three years be implemented across the debt relief spectrum, that is, for liquidation, repayment plan and NINA procedures. An automatic discharge is proposed as it will save scarce resources¹¹⁰ and as regards the period, a three-year period is chosen as lengthy terms contradict several of the primary goals of natural person insolvency which, amongst others, hold the ideal of removing disincentives to increase productivity.¹¹¹ Although some foreign jurisdictions employ shorter terms in some of their procedures, such as the one-year period in England and Wales as regards bankruptcy and the debt relief order¹¹² and the one-year period relating to the no asset procedure in New Zealand,¹¹³ a term serves moral and educational purposes¹¹⁴ and South Africa is not at a stage in its development where a more liberal term will (and should probably) be accepted. Indeed, some English scholars note that the one-year period in bankruptcy is regarded as an easy ride as compared to alternative procedures and that it may lead to the gradual erosion of social behaviour relating to the responsible use of credit.¹¹⁵ Observers in New Zealand are similarly sceptical of the short period after which a discharge becomes effective in the no asset procedure.¹¹⁶ In summary, the three-year term is chosen as it is not too distant in the future and will therefore not discourage insolvents, is in line with international principles and guidelines¹¹⁷ and tallies with previous suggestions by pertinent academics in the field.¹¹⁸ A generic period is chosen as the use of dissimilar periods in different procedures has not led to the optimal position in the

¹⁰⁸ See ch 2 par 2.7.

¹⁰⁹ See par 8.2.5.2.

¹¹⁰ Ch 3 par 3.6.

¹¹¹ See ch 2 par 2.6.2.5.

¹¹² See ch 7 para 7.3.2 and 7.4.2.

¹¹³ See ch 6 par 6.5.3.

¹¹⁴ See ch 2 para 2.6.2.5 and 2.7.

¹¹⁵ Ch 7 par 7.3.4.

¹¹⁶ Ch 6 par 6.5.3.

¹¹⁷ Ch 2 par 2.7.

¹¹⁸ See ch 3 par 3.3.4.

comparative jurisdictions.¹¹⁹ I am also of the view that debtors subject to different procedures should, in line with constitutional imperatives,¹²⁰ be treated equally as far as possible.

The conditions for an automatic discharge should not be based on a certain level of payment to creditors, which is also in line with the prohibition against discrimination on financial grounds.¹²¹ However, in keeping with the earned-start notion,¹²² I recommend that good behaviour must be set as a condition for the discharge,¹²³ although it must generally be presumed as the public only needs protection against a minority of dishonest debtors.¹²⁴ I consequently recommend that the onus should rest on creditors, insolvency practitioners, the NCR (where relevant)¹²⁵ and other interested parties, to make out a case as to why a suspension of the discharge period would be competent. This is also the case in New Zealand¹²⁶ and England and Wales,¹²⁷ although in the latter jurisdiction only the official receiver or trustee may apply for such an order which does not result in the optimal situation.¹²⁸ I recommend that insolvency practitioners and the NCR should act as guardians of public interest in insolvency matters and should not only be able, but also obliged to oppose the possibility of a discharge where public interest calls for it. In New Zealand the assignee has a duty to oppose the possibility of a discharge where the discharge would not be in the public interest.¹²⁹ Abuse of the system should justify a suspension although the factual inability to pay should not constitute a ground for such an application as was noted above. Nevertheless, and in addition to the right of interested parties to apply for the suspension of the period, I recommend that an automatic rehabilitation should not take place where a court has in any proceedings found that the insolvent acted fraudulently or is guilty of an offence in terms of insolvency legislation. An automatic rehabilitation should also not take place where it

¹¹⁹ See ch 6 par 6.5.3. and ch 7 par 7.3.4.

¹²⁰ See the general discussion of the right to equality in ch 1 par 1.1. See also par 8.1.

¹²¹ *Ibid.* See also ch 2 par 2.7 and par 8.2.7.

¹²² Par 8.2.4.1.

¹²³ See also ch 2 par 2.7.

¹²⁴ Ch 2 par 2.6.1. See also ch 7 par 7.3.4.

¹²⁵ See par 8.2.2.

¹²⁶ Ch 6 par 6.3.4.

¹²⁷ Ch 7 par 7.3.4.

¹²⁸ See ch 7 par 7.3.4.

¹²⁹ See ch 6 par 6.3.4.

is not the first time that the insolvent has been subjected to formal debt relief procedures.¹³⁰ In such instances an application should be brought to the high court which should have a wide discretion to grant or refuse the rehabilitation of the insolvent.

As was the case in England and Wales,¹³¹ I am of the view that the introduction of the recommendations in respect of a suspension of the discharge will balance the shorter period after which the automatic discharge becomes effective. The suggested instances where an automatic discharge will not be competent will further contribute to that balance.

In contemplating further and more specific procedural matters in this respect I recommend that the model of suspension and restriction orders and undertakings in England and Wales¹³² be combined, refined and streamlined. These should be incorporated in the Insolvency Act and should apply to all debt relief procedures. All such applications should be made to the high court. Where in England and Wales a restrictions order or undertaking does not affect the discharge of debt¹³³ it is submitted that, in South Africa, the combination of these instruments should result in both the limitation of the debtor's ability to re-enter the 'credit economy'¹³⁴ and the suspension of the discharge period, as such a construction will send a stronger message to dishonest or non-compliant debtors. As was pointed out above and unlike the position in England and Wales where only public officials can apply for these orders – which subjects such officials and public resources to undue strain¹³⁵ – any interested party should be able to bring such an application and guardians of public interest should be obliged to do so. As is the position in England and Wales,¹³⁶ I suggest that the maximum period for which the suspension and restrictions may run, should be provided by the Insolvency Act. Also the grounds on which such orders may be applied for should be clearly set out. These should, as is

¹³⁰ Ch 3 par 3.6.

¹³¹ See ch 7 par 7.3.4.

¹³² See ch 7 para 7.3.4 and 7.4.2.

¹³³ See ch 7 par 7.3.4.

¹³⁴ See par 8.2.4.3.

¹³⁵ Ch 7 par 7.3.4.

¹³⁶ See ch 7 para 7.3.4 and 7.4.2.

the case in England and Wales,¹³⁷ include the insolvent's failure to comply with obligations in terms of the Insolvency Act, giving preference, fraud or fraudulent breach of trust and failure to cooperate with the relevant officials or practitioners.

8.2.4.3 Scope, extent and effect of the discharge

In order to achieve effective rehabilitation and its related goals, as many debts as possible should be included in the discharge¹³⁸ as is also the case in the comparative jurisdictions.¹³⁹ However, secured debt should be excluded.¹⁴⁰ Other than that, the equal treatment of creditors does not allow for many exceptions to the discharge although debt resulting from alimony, the intentional assault or killing of another and driving under the influence of alcohol, as well as fines or a person's punishment in accordance with insolvency legislation should not be extinguished.¹⁴¹

As the South African system employs a rather wide discharge in sequestration proceedings¹⁴² it is suggested that, subject to the above submissions, it should be extended to alternative procedures as well. At the same time that the discharge becomes effective the insolvent should also be relieved of every disability relating to him being subject to a debt relief procedure. Therefore, the discharge should have an extended meaning referring to both the discharge of debt and that of restrictions, disqualifications and prohibitions relating to for instance the incurring of debt and entering certain professions. In line therewith, once a discharge becomes effective, and contrary to the present situation where information relating to a rehabilitation in sequestration proceedings remains with credit bureaux for a period of five years after the effective date,¹⁴³ all adverse information regarding to the debtor being subject to any of the debt relief procedures and all information relating to his rehabilitation should be expunged from credit bureaux. This is because the retention of such information puts the debtor's chances of a true fresh start at risk. Such retention is also contrary to international principles and guidelines¹⁴⁴ and results in discrimination

¹³⁷ See ch 7 par 7.3.4.

¹³⁸ See ch 2 par 2.7.

¹³⁹ Ch 6 par 6.3.4 and ch 7 par 7.3.4.

¹⁴⁰ *Ibid*, ch 2 par 2.7 and par 8.2.2.

¹⁴¹ Ch 3 par 3.3.4. Compare ch 6 par 6.3.4 and ch 7 par 7.3.4.

¹⁴² See ch 3 para 3.3.4 and 3.6.

¹⁴³ See ch 3 par 3.3.4.

¹⁴⁴ Ch 2 par 2.7.

after relief was granted.¹⁴⁵ I recommend that the regulations relating to the removal of adverse information as regards paid-up judgments be extended to also provide for the removal of information relating to debt relief procedures.¹⁴⁶ However, this information should be available to the registrars of the courts and to the NCR which would enable them to flag repeat applications. Where a suspension and restrictions order has been made, the information should evidently remain with the bureaux for a longer time – until the period for which the order is effective has run out.¹⁴⁷

Further relating to the effect of the discharge, the legislature should state unequivocally that it would extinguish all pre-insolvency debt and that an undertaking to pay such debt thereafter is void.¹⁴⁸

8.2.5 Multiple procedures depending on the debtor's circumstances

8.2.5.1 General procedural recommendations

a. Equality and best efforts

It has been recommended that all honest insolvent debtors should have access to the broader system.¹⁴⁹ Also, once entry to the broader system is gained debtors subject to any insolvency procedure should as far as possible be treated equally. In this respect it has been established that all such individuals should as a minimum receive a discharge as a tailpiece of insolvency procedures.¹⁵⁰ Nevertheless, a discharge must be earned and debtors must do the best that they can for a restricted period to be awarded with a discharge at the end thereof.¹⁵¹ What would be regarded as 'the best that one can do' is a factual question and the answer would differ depending on the circumstances. Asset liquidation procedures, repayment plan procedures and procedures suited to NINA debtors' needs are examples of procedures that would cater for differing circumstances and merits. Therefore and in summary, I recommend that an individual should apply for a procedure suited to his

¹⁴⁵ See para 8.2.4.1 and 8.2.7.

¹⁴⁶ See ch 1 par 1.1.

¹⁴⁷ See par 8.2.4.2.

¹⁴⁸ See ch 3 par 3.

¹⁴⁹ Par 8.2.3.

¹⁵⁰ Par 8.2.4.

¹⁵¹ Para 8.2.2 and 8.2.4.1. See also ch 2 para 2.3 and 2.7.

needs, which procedure should not result in discrimination in comparison with other procedures, and whilst the debtor is subject to the procedure his best efforts should be expected. If debtors' best efforts are required (whatever that might mean in the circumstances) for a period that is generally the same over the whole debt relief spectrum¹⁵² and if all such debtors receive a discharge at the end thereof¹⁵³ there will be little incentive for debtors to abuse certain procedures (as is happening at present)¹⁵⁴ in order to circumvent the broader system's discriminatory practices. Also, creditor resistance will be reduced¹⁵⁵ as the same value would be extracted notwithstanding the procedure to which the debtor is subject. Furthermore, if these recommendations are followed it would not be necessary to devise stringent and expensive testing and/or gate-keeping to ensure that certain procedures are not 'abused'.

b. Best efforts and different procedures

I recommend three different procedures, namely two hybrid procedures and one NINA procedure. Hybrid procedures are necessary to ensure that debtors' best efforts are collected – thereby including assets and income. Both New Zealand and England and Wales provide for the collection and distribution of income and assets in their bankruptcy and repayment plan procedures.¹⁵⁶ The South African sequestration procedure does provide for the collection and distribution of both assets and income although income is rarely collected in practice.¹⁵⁷ In turn, the administration order procedure provides for the sale of assets, although debtors entering the procedure rarely have assets of value and therefore the provision is not generally utilised – which is in order as the possibility at least exists.¹⁵⁸ However, the debt review procedure does not include a specific provision allowing for the attachment and sale of assets.¹⁵⁹ Nevertheless, two hybrid procedures are necessary as in one the focus should be on assets and in the other on income. That is not to say that assets and income payments would always be required from all

¹⁵² Par 8.2.4.2.

¹⁵³ Par 8.2.4.1.

¹⁵⁴ See ch 3 par 3.3.2. See also ch 4 par 4.3.3.

¹⁵⁵ See ch 4 par 4.3.4 as regards creditor resistance to some of the existing procedures.

¹⁵⁶ See ch 6 para 6.3 and 6.5.2 and ch 7 para 7.3.3 and 7.4.1.

¹⁵⁷ See ch 3 par 3.3.2.2.

¹⁵⁸ See ch 4 par 4.2.1.

¹⁵⁹ See ch 4 par 4.3.

debtors subject to these procedures. One procedure should be focused on assets and would be suited to those circumstances where the debtor owns assets of substantial value. Where a debtor has surplus income (that is, net earnings after essential expenses were deducted) it should also be collected for distribution. I refer to this proposed procedure as the liquidation procedure as its focus is on asset liquidation. However, such a procedure will only be implemented in the minority of natural person insolvency cases as natural person debtors rarely own valuable realisable assets. In turn, the procedure focusing on income should be suited to circumstances where the debtor has sufficient surplus income (after his and his dependants' reasonable living expenses were extracted) available for distribution, but only moderate or no non-excluded assets. Where this measure is used income and non-excluded assets of excess value should be available for distribution. This proposed procedure is referred to as the repayment plan procedure in accordance with its emphasis. Where debtors have both a steady stream of disposable income and substantial assets available, the first mentioned measure should obviously be applied as its procedures would be suited to deal with substantial estates. In the event that the debtor does not have surplus income available and does not own non-excluded valuable property, he should apply for access to the proposed NINA procedure.

As was mentioned, during the time that debtors are subject to any of the involuntary formal debt relief procedures, the same consequences should generally follow and the procedures should run for the same term, namely, three years.¹⁶⁰ Where debtors wish to circumvent restrictions, disqualifications and prohibitions applicable to formal involuntary procedures, they should be able to enter into voluntary arrangements. In this respect I submit that if the above recommendations relating to a generic period of three years for all debt relief procedures¹⁶¹ and an automatic discharge at the end of all procedures¹⁶² are implemented, creditors would theoretically be more inclined to negotiate alternatives to the more radical forced discharge. However, voluntary procedures should, due to their general inefficiency¹⁶³ and the additional

¹⁶⁰ See par 8.2.4.2.

¹⁶¹ Par 8.2.4.2.

¹⁶² Par 8.2.4.1.

¹⁶³ See ch 2 para 2.6.2.1 and 2.7.

unnecessary expenses that unsuccessful attempts bring about,¹⁶⁴ never be set as a prerequisite for entry into one of the involuntary procedures. It should for the same reasons also not be established as a precondition for a discharge as is presently suggested within the ambit of the proposed pre-liquidation composition.¹⁶⁵

c. Interplay between different procedures

When devising insolvency procedures it is important to take cognisance of general civil procedure and the interplay between insolvency law and these procedures as well as between insolvency procedures *inter se*.¹⁶⁶ The failure to properly regulate these matters in the South African natural person insolvency system has led to abundant litigation.¹⁶⁷ I recommend that, as is the case in England and Wales,¹⁶⁸ the courts and the NCR should, when deciding whether to grant an application for a particular procedure, consider whether other procedures would not be more suited to the circumstances. However, as I am proposing that the same value should be extracted from debtors irrespective of the procedure to which they are subject, the dismissal of an application for access to a particular procedure would only be necessary where the employment of that procedure will result in abuse, inefficiency or substantial waste as opposed to another. Courts and the NCR should therefore be slow to exercise this discretion. The Insolvency Act should contain clear access criteria as regards different procedures in order to assist debtors in making the choice as regards the most suited procedure. However, I am not in favour of stringent means testing. In the USA it has resulted in waste, proving to be largely ineffective in reaching its goal of curbing debtor abuse.¹⁶⁹ Nevertheless, in the USA one measure is far more attractive to debtors than the other whereas the proposals in this thesis lobby for the same level of debtor sacrifice irrespective of the procedure employed.¹⁷⁰

¹⁶⁴ See for instance the discussion in ch 5 para 5.2 and 5.9.

¹⁶⁵ Ch 5 par 5.2.

¹⁶⁶ See par 8.2.2.

¹⁶⁷ See ch 3 par 3.3.2.3 and ch 4 para 4.3.2 and 4.3.4.

¹⁶⁸ See ch 7 par 7.3.2.

¹⁶⁹ See ch 2 par 2.2.

¹⁷⁰ *Ibid.*

d. Secured credit

In line with international principles and guidelines¹⁷¹ I recommend that the rights of secured creditors should be protected throughout the debt relief spectrum.¹⁷² Further to the arguments for their exclusion as discussed in chapter 2,¹⁷³ from a practical stance and as was illustrated by the discussions of the debt review procedure in chapter 4¹⁷⁴ and court-ordered debt review in chapter 5,¹⁷⁵ the infringement of such fundamental rights leads to radical opposition and unnecessary litigation focused on technical aspects. Debtors who wish to retain non-excluded assets forming the subject of security, should either make out a reasonable argument for its consideration in living expenses¹⁷⁶ or opt for negotiated relief.

e. Ancillary matters

Adding to the general procedural recommendations above, other recommendations relevant to all procedures are that a moratorium on debt enforcement should become effective once a case has been filed¹⁷⁷ and that creditor participation should, except in cases where the estate represents significant value, be excluded.¹⁷⁸

A discussion of the specific proposed procedures follows.

8.2.5.2 Asset liquidation procedure

a. General

Although bankruptcy type procedures are generally intended for estates with low or no redemption capacity, where the focus on assets is mostly a formality,¹⁷⁹ in South Africa it is supposed to be employed by those forming part of the higher tiers of the

¹⁷¹ Ch 2 par 2.7.

¹⁷² See par 8.2.2.

¹⁷³ See ch 2 par 2.6.2.5.

¹⁷⁴ See ch 4 par 4.3.

¹⁷⁵ See ch 5 par 5.4.

¹⁷⁶ See ch 4 para 4.2.3 and 4.5.

¹⁷⁷ Ch 2 par 2.7.

¹⁷⁸ *Ibid.* See also ch 6 par 6.7 and ch 7 par 7.6.

¹⁷⁹ Ch 2 par 2.7.

economy who will in many instances have valuable property and some form of surplus income available for distribution.¹⁸⁰

Within the context of the broader reform recommendations in this thesis, I recommend the retention of the sequestration procedure with minor amendments. This is because such a procedure is necessary to liquidate assets of value in a coherent fashion even if such estates represent by far the minority of insolvency cases in South Africa at present.¹⁸¹ Also, the existing procedure is mostly efficient when employed in circumstances for which it was intended.¹⁸² Linked to the retention of the procedure for estates representing significant value and as will be further discussed below, I recommend the retention of the advantage for creditors requirement to ensure that this involved and costly procedure is mostly employed in cases where it would be viable and desirable to do so. In line with my recommendation for the procedure's retention for estates of significant value and the consequent support for the advantage for creditors requirement, creditor applications should remain. This is so since creditors should be able to invoke the procedure where it is needed to ensure an equitable and orderly distribution of assets amongst creditors in insolvent circumstances.¹⁸³

b. Regulation and administration

I recommend that the reform of the liquidation procedure should continue by retaining the procedure in the unified Insolvency Bill.¹⁸⁴ Even though a separate piece of legislation creates a better opportunity to take cognisance of the special needs of insolvent individuals,¹⁸⁵ the liquidation procedure should (if recommendations in this thesis are accepted and implemented) only be utilised in instances where an estate represents significant value and in these cases a general and unified insolvency act is better positioned to regulate intricate problems that may more readily arise from the circumstances of such estates. Complicated legal issues

¹⁸⁰ See ch 1 par 1.1 and ch 3 par 3.3.3.

¹⁸¹ Ch 1 par 1.1.

¹⁸² See ch 3 par 3.3.3.

¹⁸³ See ch 3 par 3.3.1.

¹⁸⁴ See ch 1 par 1.1.

¹⁸⁵ See ch 2 par 2.6.2.1.

may for instance result from cases where the debtor's financial difficulties have a background of business failure.¹⁸⁶

I recommend that the high courts remain involved in the liquidation procedure initially. The courts should stay involved as they are trusted institutions that are best situated to provide direction in applying the advantage for creditors standard within the context of the recommended dispensation as a whole. I am also in favour of retaining the role of the master as regards liquidation proceedings at present. However, if recommendations as regards the reduction of court involvement in alternative procedures (discussed below)¹⁸⁷ are followed and once industry has become familiar therewith, the role of the courts in liquidation proceedings should be reconsidered. If such reform is considered in future, the administrative New Zealand debtor application in bankruptcy¹⁸⁸ and the reform brought about by the Enterprise and Regulatory Reform Act¹⁸⁹ as regards debtor applications in England and Wales,¹⁹⁰ could set an example. At the same time the master's substitution with the NCR should be considered.

Although the liquidation procedure should generally only be applied to intended (valuable) estates, where liquidation would result in pecuniary benefit for creditors, the legislature should recognise that the liquidation procedure is in fact a debt relief measure and that relief is its most important aim. As was suggested above and contrary to the present position where the discharge is regarded as a mere consequence of the procedure,¹⁹¹ an objects clause should clearly state that debtors' economic rehabilitation is the main objective thereof although, within this all-encompassing object, the system strives to achieve a balance between the rights of the debtor, creditors and society at large.¹⁹²

¹⁸⁶ *Ibid.*

¹⁸⁷ See para 8.2.5.3 and 8.2.5.4.

¹⁸⁸ See ch 6 par 6.3.2.

¹⁸⁹ 2013.

¹⁹⁰ See ch 7 par 7.3.1.

¹⁹¹ Ch 3 par 3.3.1.

¹⁹² See par 8.2.2.

c. Access

As regards substantive requirements and within broader reform objectives, I propose that only the inability to service debt and the advantage for creditors requirement should be set. Notwithstanding strong criticism against the latter requirement,¹⁹³ it serves important purposes and I therefore recommend its retention.¹⁹⁴ If proper alternative procedures leading to a discharge are devised,¹⁹⁵ as is suggested in this thesis,¹⁹⁶ debtors excluded from the sequestration procedure would no longer be marginalised by the advantage requirement which would save the requirement from unconstitutionality.¹⁹⁷ Consequently, the Law Reform Commission's proposals to ensure that the advantage requirement is met, by for instance requiring a provisional order and that security be set, are supported.¹⁹⁸ However, contrary to what the commission is proposing at present, the onus to prove that another procedure would not be more useful in the circumstances should not as a matter of course rest on the debtor. It is suggested that creditors should rather be able to oppose applications on the strength thereof, but then they should prove that it would probably be the case.¹⁹⁹ Nonetheless, if recommendations to ensure that best efforts are harvested,²⁰⁰ irrespective of the procedure employed, are implemented, creditors should theoretically be able to obtain as much value from the sequestration procedure as in alternative measures and therefore opposition would probably not occur in many instances.

In line with my support for the advantage for creditors requirement coupled with the fact that the sequestration procedure is intended to ensure a fair and orderly distribution to creditors where real value exists, I have recommend that creditor applications remain. Such applications are also allowed in New Zealand²⁰¹ and England and Wales²⁰² where the courts are still involved in such petitions.²⁰³

¹⁹³ Ch 3 par 3.3.2.2.

¹⁹⁴ Ch 3 para 3.3.1 and 3.5.

¹⁹⁵ See par 2.5

¹⁹⁶ See para 8.2.5.3 and 8.2.5.4.

¹⁹⁷ See ch 3 par 3.5.

¹⁹⁸ See ch 3 par 3.3.2.1.

¹⁹⁹ Ch 4 par 4.3.4.

²⁰⁰ Par 8.2.5.1.

²⁰¹ See ch 6 para 6.3.1 and 6.3.2.

²⁰² See ch 7 para 7.3.1 and 7.3.2.

²⁰³ See ch 6 par 6.3.2 and ch 7 par 7.3.2.

However, I suggest that creditor applications in South Africa, in contrast with the situation at present,²⁰⁴ should be reviewed more stringently by the courts not least as in such instances creditors apply for orders that affect a debtor's person. In this respect I refer to the comparative jurisdictions where the absence of assets in creditor petitions, as opposed to debtor petitions, play a role when the court exercises its discretion in deciding whether to allow or refuse the petition.²⁰⁵ Although South African courts' initiatives to more intensely scrutinise voluntary applications as opposed to compulsory ones are probably defensible within the current dispensation where the legislation's objectives are skewed in favour of creditors²⁰⁶ and also as creditors do not have the same level of knowledge of debtors' financial affairs as debtors themselves,²⁰⁷ the balance that my recommendations seek to achieve would require a fresh approach. However, while creditor applications should generally be allowed, it should not be competent in instances where another debt relief measure is in force and is complied with.²⁰⁸ Nevertheless, it is suggested that, if recommendations as regards best efforts and the exclusion of secured debt are heeded,²⁰⁹ creditors may not find such endeavours attractive in future.

Relating to the inability to pay requirement and within the realm of creditor applications, acts of bankruptcy should not form part of the process as is duly proposed in the 2015 Insolvency Bill.²¹⁰ This is because the focus should be on the inability to pay and not on debtors' wrongful actions.²¹¹ The commission's proposal relating to the introduction of a statutory demand to replace the out-dated notion of acts of insolvency is supported.²¹² Evidence that such initiatives are fruitful emanates from England and Wales where a similar construction has simplified and clarified the

²⁰⁴ Ch 3 par 3.3.2.

²⁰⁵ See ch 6 par 6.3.2 and ch 7 par 7.3.2.

²⁰⁶ See ch 3 par 3.3.2.2.

²⁰⁷ See ch 4 par 4.3.4.

²⁰⁸ Ch 4 par 4.5.

²⁰⁹ Par 8.2.5.1.

²¹⁰ See ch 3 par 3.3.2.1.

²¹¹ See ch 2 para 2.6.2.3 and 2.7.

²¹² See par 3.3.2.1.

area of law.²¹³ However, such reforms should truly be focused on inability to pay and should not echo acts of insolvency that are focused on wrongful actions.²¹⁴

d. Other procedural aspects

As regards procedural matters other than those discussed above, a moratorium on debt enforcement should become effective the moment an application is filed²¹⁵ contrary to the position at present where a sequestration order results in such a moratorium.²¹⁶

As estates subject to the liquidation procedure would represent real value, creditor participation is logical and coincides with the international principle that such participation should be allowed (only) in such instances.²¹⁷ I therefore recommend that creditor participation, as is provided for in the sequestration procedure,²¹⁸ should remain.

Although the Insolvency Act provides for the collection and distribution of income it is rarely used in practice.²¹⁹ I recommend that this measure should be strengthened. In this respect the insolvency practitioner should be obliged to conduct an investigation as to the surplus amount of income to be attached and distributed. I propose that either the master make such an order (as is presently the position)²²⁰ or that the debtor may agree thereto (which will save costs) as is the case in England and Wales.²²¹ This proposal is in line with the view that those who are subject to debt relief procedures should do the best that they can for a restricted period of time to earn the discharge at the end of the period.²²² The 2015 Insolvency Bill proposes a procedure that the liquidator may follow to bring a debtor before a magistrate (in chambers) to supply proof of assets and income and estimated expenses for his own

²¹³ See ch 7 par 7.3.2.

²¹⁴ See ch 3 par 3.3.2.1 and ch 2 par 2.7.

²¹⁵ See ch 2 par 2.7.

²¹⁶ Ch 3 par 3.3.1.

²¹⁷ See ch 2 par 2.7.

²¹⁸ Ch 3 par 3.3.

²¹⁹ Ch 3 par 3.3.2.2.

²²⁰ *Ibid.*

²²¹ See ch 7 par 7.3.3.

²²² See para 8.2.2 and 8.2.5.1.

support and that of his dependants.²²³ In line with the goal of reducing court involvement²²⁴ and as was recommended, this function should rather be fulfilled by the master. Also, a uniform standard is in this respect recommended as it will ease such an inquiry and save scarce resources.²²⁵ This also ties in with the discussion below relating to the calculation of the amount to be attached.²²⁶

e. *Discharge*

Although in some jurisdictions, such as England and Wales,²²⁷ an argument can be made that liquidation procedures should run for shorter periods than those that apply in repayment plan procedures – as there is no benefit in extending them – it is not relevant in the South African context where, due to the proposed liquidation procedure's entry requirements, there will be a substantial estate to liquidate and possibly also surplus income to distribute. Further, a term serves important educational purposes.²²⁸ Also and as was explained above, a difference in the periods for which different procedures will be effective will result in inequality and further unwanted consequences.²²⁹ Therefore, I again suggest the generic three-year term as regards the liquidation procedure.²³⁰

When considering the exclusion and/or exemption of property it should be kept in mind that it is directly linked to the debtor's rehabilitation and the probability of him making a fresh start.²³¹ However, probably due to the Insolvency Act's present focus on the advantage for creditors requirement *per se*, both the current and proposed exclusion and exemption regimes are sorely lacking.²³² Nevertheless, although international principles and guidelines favour a standards-based approach that excludes most property from the estate as a matter of course in jurisdictions where

²²³ See ch 3 par 3.3.3.

²²⁴ Ch 2 par 2.7.

²²⁵ *Ibid.*

²²⁶ Par 8.2.4.3.

²²⁷ Ch 7 par 7.2 and 7.3.4.

²²⁸ Par 8.2.4.1.

²²⁹ See ch 2 para 2.6.2.5 and 2.7. See also par 8.2.4.

²³⁰ Par 8.2.4.2.

²³¹ Par 8.2.4.1.

²³² Ch 3 para 3.3.3 and 3.6.

debtors have limited personal assets²³³ – such as in South Africa²³⁴ – the liquidation procedure would by definition only allow access to those who do in fact own property of considerable value. Therefore, such a standard is not suited to the South African liquidation procedure. However, this does not mean that the exclusion/exemption regime is not in need of an overhaul. In fact the opposite is true due to, amongst others, the recommended balance between the advantage for creditors requirement and the economic rehabilitation of the debtor with the latter taking centre stage.²³⁵ As regards housing specifically, it is strange that the Law Reform Commission did not take cognisance of the constitutional imperatives relating to housing and the possible impact thereof on natural person insolvency procedures.²³⁶

Nevertheless, save for adding my voice to the call for a drastic modernisation of the exclusion/exemption regime, this thesis is not focused on these aspects *per se*. Therefore, the doctoral research by Steyn entitled *Statutory regulation of forced sale of the home in South Africa* and particularly her proposals in the context of natural person insolvency law and that by Evans entitled *A critical analysis of problem areas in respect of assets of insolvent estates of individuals*, should provide a firm basis from which the commission should devise proper policy in this regard.²³⁷ These policies should not only extend to the liquidation procedure, but also to alternative procedures.²³⁸ Nevertheless, the commission's attempt to bring excluded property in line with that contained in the Supreme Court Act²³⁹ and the Magistrates' Courts Act²⁴⁰ is applauded as such harmony will result in a fairer and more certain legal environment generally. However, these are sadly lacking in themselves and should form part of the larger reform.²⁴¹

²³³ Ch 2 par 2.7.

²³⁴ Ch 1 par 1.1 and par 8.2.1.

²³⁵ Par 8.2.2.

²³⁶ Ch 3 para 3.3.3 and 3.6.

²³⁷ See also ch 3 par 3.3.3.

²³⁸ Para 8.2.5.3 and 8.2.5.4.

²³⁹ 59 of 1959.

²⁴⁰ 32 of 1944. See ch 3 par 3.3.3.

²⁴¹ Ch 3 par 3.3.3.

8.2.5.3 Repayment plan procedure

a. General

Although there are doubts as to whether repayment plans are effective in achieving the goals of natural person insolvency, they serve important moral and educational purposes.²⁴² These procedures are therefore in line with the preferred earned start principle,²⁴³ where debtors are expected to do the best that they can for a restricted period of time to be awarded with a discharge after such period.²⁴⁴ Repayment plan procedures are further warranted as it would be unfair and unreasonable to expect of debtors qualifying for the liquidation procedure to surrender their surplus value for distribution amongst creditors but not to expect the same from those without substantial assets, but who have surplus income available for distribution.²⁴⁵ I therefore recommend a repayment plan procedure for South Africa.²⁴⁶

The existing South African repayment plan procedures, namely the administration order²⁴⁷ and debt review²⁴⁸ procedures are insufficient in many respects²⁴⁹ and I consequently recommend that these procedures be repealed and that a single repayment plan procedure be devised.²⁵⁰ In line with *Boraine et al*²⁵¹ I suggest that the new procedure should be based on the well-established debt review system which is regulated by the NCR and where accredited and regulated payment distribution agencies effect the necessary distributions.²⁵² However, I hold the view that the administration order procedure sports superior procedural attributes. One such example is the manner in which the procedure attains a balance between the rights of debtors and creditors as regards secured assets and especially mortgage bonds.²⁵³

²⁴² Ch 2 par 2.7.

²⁴³ See para 8.2.1, 8.2.2 and 8.2.4.1.

²⁴⁴ Ch 2 par 2.7.

²⁴⁵ See par 8.2.5.2 and the general discussion of the right to equality in ch 1 par 1.1.

²⁴⁶ Par 8.2.5.1.

²⁴⁷ See ch 4 par 4.2.

²⁴⁸ See ch 4 par 4.3.

²⁴⁹ See ch 4 par 4.5.

²⁵⁰ *Ibid.*

²⁵¹ *Boraine et al* 2012 *De Jure* 269–270.

²⁵² See ch 4 para 4.3.6 and 4.5.

²⁵³ Ch 4 para 4.2.3, 4.3.6 and 4.5.

b. Regulation and administration

I recommend that the proposed repayment plan procedure should form part of the current insolvency law reform process.²⁵⁴ It was also recommended that the proposed procedure be incorporated in the unified Insolvency Bill, which (as was submitted above)²⁵⁵ should resort under the Department of Trade and Industry.

As regards court involvement in the proposed repayment plan procedure, I recommend that, in line with international principles and guidelines,²⁵⁶ their functions should constitute the exception rather than the rule. If this recommendation is accepted the pertinent issue revolves around the best institution to oversee the proposed measure. Related to this consideration is the existing physical infrastructure as this should be built upon.²⁵⁷ Institutions (other than the courts) which are suited to deal with matters related to natural person insolvency are the master of the high court and the NCR, although neither of these institutions have a wide national footprint. However, as the NCR is already accustomed to the environment – it regulates the part of the credit industry that has a bearing on natural persons and also the debt review procedure specifically²⁵⁸ – I have recommend that it oversee the suggested repayment plan procedure.²⁵⁹ The NCR also (already) resorts under the recommended government department, namely the Department of Trade and Industry.²⁶⁰ As regards infrastructure, a national footprint is found in police services, municipalities and the courts. Law enforcement and municipalities are far removed from insolvency matters and therefore magistrates' courts, which are presently involved in the administration and debt review procedures,²⁶¹ remain. I consequently recommend that offices of the NCR should be adjunct to the magistrates' courts. A similar alliance is found in England and Wales where offices of the public official receiver is attached to the courts.²⁶²

²⁵⁴ See ch 1 par 1.1. See also par 8.2.2.

²⁵⁵ Par 8.2.2.

²⁵⁶ Ch 2 par 2.7.

²⁵⁷ *Ibid.*

²⁵⁸ See ch 4 par 4.3.2 as regards the NCR.

²⁵⁹ Par 8.2.2.

²⁶⁰ *Ibid.*

²⁶¹ See ch 4 para 4.2.1 and 4.3.2.

²⁶² See ch 7 par 7.3.1.

Although it is recommended that the NCR's functions be expanded to oversee the proposed repayment plan procedure, I recommend that insolvency practitioners should remain involved and should supervise debtors' compliance with the proposed repayment plan procedure, as is presently the case with the administration order²⁶³ and the debt review²⁶⁴ procedures. This is also the position in the New Zealand summary instalment order procedure.²⁶⁵ However, the well-established payment distribution agencies that are already registered with and regulated by the NCR and that presently distribute payments in accordance with the debt review procedure,²⁶⁶ should collect and distribute funds in terms of the recommended repayment plan procedure. It is submitted that this feature is a positive attribute of the present debt review procedure compared to the administration order procedure.²⁶⁷

I recommend that the existing and entrenched fee structures relating to payment distribution agencies and debt counsellors be employed in the proposed repayment plan procedure.²⁶⁸ As far as the NCR's fees are concerned, the New Zealand assignee receives 2.5% of collected value in summary instalment orders.²⁶⁹ I recommend that the NCR should similarly be funded through a percentage of funds periodically collected by payment distribution agencies, but that a study concerning the desired percentage should be undertaken.

c. Access

I recommend that only debtor applications should be allowed. This is also generally the position in New Zealand where creditors may only apply for summary instalment orders with debtors' consent.²⁷⁰

I recommend that debtors should apply to the NCR for access to the proposed repayment plan procedure by making use of an insolvency practitioner. An application fee should be paid which should, in addition to the percentage deducted

²⁶³ Ch 4 par 4.2.4.

²⁶⁴ Ch 4 par 4.3.2.

²⁶⁵ See ch 6 par 6.5.2.

²⁶⁶ Ch 4 para 4.3.2, 4.3.6 and 4.5.

²⁶⁷ See ch 4 para 4.2.4 and 4.3.6.

²⁶⁸ See ch 4 par 4.3.2.

²⁶⁹ Ch 6 par 6.5.2.

²⁷⁰ *Ibid.*

from periodic payments, contribute to financing the offices of the NCR. The application must be accompanied by a proposed repayment plan (which should generally be drawn up by an insolvency representative) and supporting documents that should adhere to standardised norms. I recommend that the application should be submitted either electronically or at the NCR's offices at the magistrates' courts.

Unlike the various access requirements found in the two existing secondary procedures at present,²⁷¹ I recommend that the only substantive entry requirements as regards the proposed repayment plan procedure should be the inability to pay existing debt, the availability of surplus income for distribution and that the debtor would not readily satisfy the advantage for creditors requirement – which would make him eligible for the liquidation procedure specifically.²⁷² However, as was pointed out above,²⁷³ I recommend that it should be possible to extract the same value from debtors irrespective of whether the liquidation or repayment plan procedure is employed and therefore the NCR should not lightly deny access to the repayment plan procedure. Nevertheless, where the NCR is of the opinion that the estate represents significant value and that such value would probably only be distributed in an orderly and fair manner if the liquidation procedure is employed,²⁷⁴ it should dismiss the application.

d. Other procedural aspects

As is presently the case with the debt review procedure,²⁷⁵ but not the administration order procedure,²⁷⁶ I recommend that a moratorium on debt enforcement should become effective the moment an application for the repayment plan procedure is filed with the NCR.²⁷⁷ This is also the internationally preferred position.²⁷⁸

²⁷¹ See ch 4 para 4.2.2 and 4.3.3.

²⁷² See par 8.2.5.2.

²⁷³ Par 8.2.5.1.

²⁷⁴ Par 8.2.5.2.

²⁷⁵ Ch 4 par 4.3.2.

²⁷⁶ Ch 4 par 4.2.1.

²⁷⁷ Par 8.2.5.1.

²⁷⁸ Ch 2 par 2.7.

As regards plan formulation, I recommend that rules be employed²⁷⁹ and that the focus of such rules should be on the debtor's level of sacrifice, rather than benefit for creditors, as is recommended by international principles and guidelines.²⁸⁰ Further in consonance with international principles and guidelines,²⁸¹ the process should prescribe that the calculation ought to commence with a determination of the amount that needs to be reserved for the maintenance of the debtor and his dependants. Unlike the position at present in terms of the administration order and debt review procedures,²⁸² a standardised approach is suggested, as sacrifice in exchange for relief is an inherent political decision that should be made by the legislature.²⁸³ Also, to determine the surplus level for distribution in every case is a costly and timeous endeavour. However, a measure of discretion is still needed and a standard baseline should be supplemented by non-standard allowances such as housing, transport and child care.²⁸⁴ Although many jurisdictions view the insolvency system as an extension of the ordinary collection system where the same limitations on the garnishment of wages and other income are adopted,²⁸⁵ in South Africa no limitations as regard the percentage of income that may be attached in individual enforcement proceedings is prescribed.²⁸⁶ I therefore, in line with international principles and guidelines,²⁸⁷ suggest that bands of uniformity, where people are categorised into groups with different excluded amounts in accordance with for example the number of dependent children and their ages, are developed and that these be uniformly employed in all natural person insolvency procedures. It is submitted that general standards relating to living expenses as were drawn up by the credit industry forum²⁸⁸ could be considered as a starting point in the development of such a model which should also be in line with affordability assessment regulations.²⁸⁹ Further as regards living expenses, it should be possible, as is

²⁷⁹ *Ibid.*

²⁸⁰ *Ibid.*

²⁸¹ *Ibid.*

²⁸² Ch 4 para 4.2.1 and 4.3.2.

²⁸³ Ch 2 par 2.7.

²⁸⁴ See ch 2 par 2.6.2.5.

²⁸⁵ *Ibid.*

²⁸⁶ See ch 1 par 1.1.

²⁸⁷ Ch 2 par 2.6.2.5.

²⁸⁸ See ch 4 par 4.3.2.

²⁸⁹ See ch 5 par 5.5.

presently the case in terms of the administration order procedure,²⁹⁰ to provide for periodical payments in terms of a mortgage bond (especially where it represents the debtor's home) in the debtor's living expenses. In this manner a just balance between the interests of the credit provider and the debtor could be reached. The same should apply to periodical instalments relating to excluded items²⁹¹ bought on credit. However, as is the position in terms of the administration order procedure at present,²⁹² cognisance should be taken of all relevant circumstances to determine the reasonableness of such payments.

To determine future income, I recommend that a projection should be used as the actual income approach will result in significant monitoring and administrative costs,²⁹³ which are not ideal in an exercise intended to salvage what is left. Income derived from government-based social assistance (social grants)²⁹⁴ should not be channelled to creditors. Nevertheless, it should be taken into account in determining the surplus amount payable. In other words, it will (only) be a problem when debtors are solely dependent on government grants and these are diverted to creditors.²⁹⁵ However, debtors receiving assistance would more regularly resort under the NINA procedure in any event.²⁹⁶

I recommend that, in line with international principles and guidelines,²⁹⁷ creditor participation in claim verification and plan formulation should not be required and should be excluded as a matter of course.²⁹⁸ However, creditors should be able to approach the NCR with queries relating to claims and the magistrate's court if they seek a review of the plan or wish to appeal a decision of the NCR.

I recommend that the NCR be able to electronically verify certain information and that it should consequently have access to a wide variety of data bases. In this

²⁹⁰ See ch 4 par 4.2.1.

²⁹¹ Par 8.2.5.2.

²⁹² Ch 4 par 4.2.3.

²⁹³ See ch 2 par 2.6.2.5.

²⁹⁴ See ch 1 par 1.1.

²⁹⁵ See ch 2 par 2.6.2.5.

²⁹⁶ Par 8.2.5.4.

²⁹⁷ Ch 2 par 2.7.

²⁹⁸ See par 8.2.5.1.

respect and as a minimum it should verify the debtor's active credit agreements, whether immovable property is registered in the debtor's name and, where relevant, details regarding the debtor's income at the South African Revenue Services. Once the NCR has applied its mind to the application and has verified the prescribed information, it should endorse, amend or reject the repayment plan. The NCR's decision should have the same status as a court order and, where the debtor is a salaried worker, should be coupled with (as is the case in the administration order procedure at present)²⁹⁹ a direction that the monthly surplus income be deducted and paid over by the employer to the relevant payment distribution agency. The employer should not be able to charge fees for this uncomplicated function. Where a plan is rejected, the debtor should be able to approach the court for a review.

As is provided for in the administration order procedure,³⁰⁰ I recommend that the repayment plan procedure should clearly stipulate that plan modification is possible in instances where the debtor experiences a drastic change in his financial circumstances. This recommendation is in line with international principles and guidelines.³⁰¹

e. *Discharge*

The recommended generic standard period of three years from date of application until the automatic discharge is received should obviously also apply to the repayment plan procedure.³⁰² The same holds true for the debts that should be discharged and the consequences of a discharge.³⁰³

It is apparent from international principles and guidelines that the debtor's ability to retain property improves the outcome of the discharge as debtors are provided with the necessities to continue with their lives.³⁰⁴ For this reason and the fact that debtors accessing the proposed repayment plan procedure should by definition not

²⁹⁹ Ch 4 par 4.2.1.

³⁰⁰ See ch 4 par 4.2.1.

³⁰¹ Ch 2 par 2.6.2.5.

³⁰² Par 8.2.4.2.

³⁰³ Par 8.2.4.3.

³⁰⁴ Ch 2 par 2.7.

be able to readily satisfy the advantage requirement in liquidation proceedings³⁰⁵ (and would consequently have no or only limited assets available for distribution) I recommend a standards-based approach where all property is as a matter of course excluded from the estate. I recommend that the obligation to claim non-excluded assets of excess value³⁰⁶ should, as is prescribed by international principles and guidelines,³⁰⁷ be placed on the insolvency representative. In this respect I recommend that the insolvency practitioner should be obliged to investigate whether the debtor possesses valuable assets susceptible to collection and distribution.

My last specific recommendation as regards the repayment plan procedure is the implementation of a procedure similar to the American hardship discharge.³⁰⁸ I recommend that a debtor should be able to apply to the NCR for a hardship discharge where he has accessed the repayment plan procedure, but has subsequently become a NINA debtor. The American procedure's three requirements can be transplanted to the South African system as is, as they offer a practical solution to a practical problem and no nation-centric reasons exist for them to be amended. The requirements are that:

- a. the debtor's failure to complete the plan is due to circumstances for which he should not be held accountable;
- b. creditors have received at least the liquidation value of their unsecured claims – this requirement will only be relevant where the debtor possesses some valuable asset(s) that may be claimed for distribution; and
- c. modification of the plan is not practicable.

8.2.5.4 NINA procedure

a. General

The introduction of a NINA procedure is a non-negotiable necessity within the South African context and as is the case in New Zealand³⁰⁹ and England and Wales,³¹⁰ I recommended that a free-standing NINA procedure be devised and included in the

³⁰⁵ Par 8.2.5.2.

³⁰⁶ See *ibid.*

³⁰⁷ Ch 2 par 2.7.

³⁰⁸ See ch 2 par 2.2.

³⁰⁹ See ch 6 par 6.5.3.

³¹⁰ See ch 7 par 7.4.2.

Insolvency Act. This is because none of the existing³¹¹ or recommended procedures³¹² are suited to NINA debtors' needs and experience in the comparative jurisdictions have revealed that it is not ideal to channel NINA debtors through procedures that are not customised to the NINA category's needs.³¹³ Although the proposed pre-liquidation composition was devised with, amongst others, the NINA category in mind it will unfortunately not reach its goal of assisting NINA debtors.³¹⁴ This is mainly so since the proposed pre-liquidation composition procedure in essence reflects negotiated relief and NINA debtors do not have any negotiating power.³¹⁵

I recommend that the New Zealand no asset procedure should be used as a baseline to develop the proposed NINA procedure.³¹⁶ This is because there is evidence of its effectiveness³¹⁷ and it is generally uncomplicated and therefore also relatively inexpensive.³¹⁸ Also early indications of the effectiveness of the debt relief order procedure in England and Wales that was based on the New Zealand no asset procedure are documented.³¹⁹ Recommendations that follow are therefore mostly based on the New Zealand no asset procedure.³²⁰ Proposals only relate to the most important aspects as regards the proposed procedure and are not intended as a detailed framework.

b. Regulation and administration

As is preferred by international principles and guidelines,³²¹ and was recommended within the ambit of the repayment plan procedure,³²² I recommend that courts should not as a matter of course be involved in the proposed NINA procedure. In this respect I recommend that the NCR should oversee the suggested NINA procedure

³¹¹ See ch 3 par 3.3 and ch 4 par 4.5.

³¹² Para 8.2.5.2 and 8.2.5.3.

³¹³ See ch 6 par 6.5.3 and ch 7 par 7.4.2.

³¹⁴ See ch 5 para 5.2 and 5.9.

³¹⁵ *Ibid.*

³¹⁶ See ch 6 par 6.5.3.

³¹⁷ *Ibid.*

³¹⁸ See ch 6 par 6.7.

³¹⁹ See ch 7 par 7.4.2.

³²⁰ Ch 6 par 6.5.3.

³²¹ Ch 2 par 2.7.

³²² Par 8.2.5.3.

as was also recommended for the repayment plan procedure.³²³ However, in contrast with recommendations as regards the proposed repayment plan procedure,³²⁴ I recommend that the NCR should also administer the proposed procedure. This is because no strong charitable organisations are at present ideally situated to fulfil this need and the profit-making private sector would not be interested in severely destitute debtors. The benefits of the NCR taking care of the administrative processing are that it can provide a steady bureaucracy and develop skill in identifying and sorting cases.³²⁵ It can also offer independent advice and information and deter abuse.³²⁶

c. Access

I recommend that, as is the case in New Zealand,³²⁷ debtors should meet financial requirements and requirements relating to conduct. As regards the financial requirements, the debtor should not have any valuable realisable non-excluded assets³²⁸ and no surplus income³²⁹ available for distribution amongst creditors. Although thresholds relating to the total debt are set in New Zealand,³³⁰ I am not in favour thereof as such restrictions would have the effect of excluding worthy cases from any form of relief. However, the NCR should be empowered to refer cases where substantial amounts of debt are involved for an inquiry by making use of the processes of the liquidation procedure. Also in dissonance with the New Zealand procedure³³¹ I do not recommend that debtors should only be able to access the NINA procedure once during their lifetimes, as this requirement is not set in other procedures. However, I recommend that the debtor should be disqualified from entry for the following reasons that are based on the New Zealand procedure:³³²

- a. if he has concealed assets with the intention to defraud creditors;
- b. if he has engaged in conduct that would constitute an offence under the Act;

³²³ *Ibid.*

³²⁴ *Ibid.*

³²⁵ See ch 2 par 2.6.2.2.

³²⁶ *Ibid.*

³²⁷ Ch 6 par 6.5.3.

³²⁸ See par 8.2.5.2.

³²⁹ See par 8.2.5.3.

³³⁰ See ch 6 par 6.5.3.

³³¹ *Ibid.*

³³² *Ibid.*

- c. if he has incurred debt or debts whilst knowing that he does not have the means to repay such debts; or
- d. where there is a likelihood that he would qualify for the liquidation or repayment plan procedure.

As was suggested, the debtor should apply to the NCR for access to the proposed NINA procedure. Such applications should be made by using a prescribed standardised form, which should be submitted either electronically or physically at the NCR's offices at the magistrates' courts.³³³ I recommend that officials at the offices of the NCR should assist debtors with their applications if needed. A statement of the debtor's financial affairs coupled with supporting documents should accompany the application form. Only a minimal standard fee should be required, as debtors qualifying would not be able to pay a substantial fee and such a requirement would once again exclude many NINA debtors from any form of recourse.

d. Other procedural aspects

Once the debtor has applied for access to the proposed NINA procedure a moratorium on debt enforcement should become effective³³⁴ and the NCR should forward an electronic notice of the application to all known creditors and credit bureaux. A brief summary of the debtor's financial affairs, in a prescribed format, should accompany the notice to creditors. Once the application is lodged the debtor should not be able to apply for any credit.³³⁵

The NCR must verify the information contained in the application, as far as it is practical to do so, and determine whether the debtor adheres to entry requirements. Creditor participation should be excluded as these estates do not represent value.³³⁶ If the NCR is satisfied that the access criteria are met, the debtor must be admitted to the procedure and both the debtor and creditors must be informed. I recommend that, as is suggested by international principles and guidelines,³³⁷ the NCR should make use of technology to reduce processing and error costs. Also, the responsible

³³³ See par 8.2.5.3.

³³⁴ See ch 2 par 2.7. See also par 8.2.5.1.

³³⁵ See in general ch 6 par 6.5.3.

³³⁶ Ch 2 par 2.7.

³³⁷ See ch 2 par 2.6.2.2.

officials should have costless access to credit bureaux³³⁸ and other government departments or institutions should grant them easy access to (other) registers that may hold valuable information.

As is the position in the New Zealand no asset procedure,³³⁹ I recommend that the debtor should comply with statutory duties. These are to meet reasonable requests by the NCR to provide assistance, documents and other information necessary for applying the procedure to the debtor and to notify the NCR as soon as possible of a change in circumstances that would allow him to repay an amount towards the debts subject to the procedure. As was already mentioned, the debtor should not obtain any further credit whilst he is subject to the procedure.

e. Discharge

If the procedure is not terminated on grounds discussed hereunder, the debtor should receive an automatic discharge after three years from the date on which the debtor was admitted thereto – as is also recommended for other proposed procedures.³⁴⁰ The suggested period constitutes a deviation from the New Zealand procedure for reasons mentioned above³⁴¹ and as the brevity of the twelve-month period in New Zealand receives fair criticism.³⁴²

In line with the position in New Zealand,³⁴³ I recommend that it should be possible to terminate the proposed NINA procedure at an earlier stage. This should be where the debtor was wrongly admitted to the procedure or where the debtor's financial circumstances have changed to such an extent that he can repay an amount towards his debt. A creditor should be able to apply to the NCR for termination on these grounds. Once the NCR ordered a termination it should inform the debtor and known creditors and such termination should lift the moratorium on debt enforcement. The debtor should be liable for penalties and interest that may have accrued whilst the procedure was in force.

³³⁸ *Ibid.*

³³⁹ *Ibid.*

³⁴⁰ See para 8.2.4, 8.2.5.2 and 8.2.5.3.

³⁴¹ Par 8.2.4.2.

³⁴² See ch 6 par 6.5.3.

³⁴³ *Ibid.*

8.2.5.5 *Negotiated debt relief solutions*

As regards formal versus informal procedures it was established that negotiated workouts are not preferred.³⁴⁴ Nevertheless, I recommended that where debtors experience an inability to pay and where they wish to circumvent the restrictions, disqualifications and prohibitions applicable to one of the proposed formal procedures, they should be able to enter into voluntary arrangements.³⁴⁵ In this regard the statutory composition in terms of section 119 of the Insolvency Act is a (theoretically) valuable tool at the disposal of debtors who can put forward an attractive offer compared to what would materialise in terms of the formal sequestration procedure.³⁴⁶ By making use of this procedure further costs can be minimised, which could yield a better return for creditors, and creditors may receive a dividend much earlier. From the debtor's point of view it may be beneficial as he can regain some of his assets and in some instances apply for earlier rehabilitation.³⁴⁷ The procedure mostly adheres to international principles and guidelines³⁴⁸ as it is backed by formal procedures should it fail, renders passive creditors bound to a settlement and protects secured creditors' interests.³⁴⁹ Unfortunately, passive creditors are at present allowed to hinder such agreements.³⁵⁰ The 2015 Insolvency Bill proposes a refinement of the procedure³⁵¹ and in this respect all the proposals contained in the Bill are supported. The latter proposals include that the percentage of creditors' votes be reduced and that, in line with international principles and guidelines,³⁵² only concurrent creditors who vote will be reckoned into the required majority vote. It is further suggested that the 50-cents requirement should be abandoned. Also, it is proposed that the liquidator may approach the court for the cancellation of a composition under certain circumstances.³⁵³ However, in addition to the commission's proposals I recommend that the creditors' vote should be reduced even further to a mere majority in value and in number. Also, as is the case with the

³⁴⁴ See ch 2 par 2.7. See also par 8.2.1.

³⁴⁵ See par 8.2.5.1.

³⁴⁶ See ch 3 para 3.4 and 3.6.

³⁴⁷ See ch 3 par 3.6.

³⁴⁸ Ch 2 par 2.7.

³⁴⁹ Ch 3 para 3.4 and 3.6.

³⁵⁰ *Ibid.*

³⁵¹ *Ibid.*

³⁵² Ch 2 par 2.7.

³⁵³ Ch 3 para 3.4 and 3.6.

individual voluntary arrangement in England and Wales,³⁵⁴ it should be possible to employ the statutory composition at any time and not only after the sequestration procedure is in motion.³⁵⁵ Where the composition is invoked before other debt relief procedures are employed, a moratorium on debt enforcement should become effective the moment the debtor applies for the statutory composition.³⁵⁶ I further recommend that, in line with earlier proposals,³⁵⁷ the NCR as opposed to the master should oversee the process and certify a composition. This suggestion also tallies with the recommendation that an application for the composition should be possible before and after formal non-negotiated procedures were instituted. Where the composition fails, the debtor should obviously, in accordance with his circumstances, be capable of applying for one of the proposed non-negotiated debt relief options.³⁵⁸

Another negotiated procedure, namely the proposed pre-liquidation composition, was evaluated.³⁵⁹ Although the Law Reform Commission's proposal is intended, in line with international developments in natural person insolvency law,³⁶⁰ to afford those who do not qualify for liquidation proceedings with an opportunity to attain a fresh start it has been established that it will not reach this goal.³⁶¹ It has also been found that the procedure in its current form is more suited to the needs of those natural person insolvents that already have some form of statutory recourse at their disposal.³⁶² It was consequently recommended that the proposed NINA procedure rather be implemented to cater specifically for this group's needs.³⁶³ I accordingly recommend that the proposed pre-liquidation composition procedure be removed from the Insolvency Bill and that the proposed reform of the statutory composition should be further refined. This will result in a more simplified approach.

³⁵⁴ See ch 7 par 7.4.1.

³⁵⁵ Ch 3 para 3.4 and 3.6.

³⁵⁶ Ch 2 par 2.7.

³⁵⁷ See para 8.2.2, 8.2.5.3 and 8.2.5.4.

³⁵⁸ See para 8.2.5.2, 8.2.5.3 and 8.2.5.3.

³⁵⁹ See ch 5 para 5.2 and 5.9.

³⁶⁰ Ch 2 par 2.7.

³⁶¹ See ch 5 para 5.2 and 5.9.

³⁶² *Ibid.*

³⁶³ See par 8.2.5.4.

8.2.6 Financing issues

As South Africa is a developing country I recommend that the system should as far as possible be self-financing. However, as is suggested by international principles and guidelines,³⁶⁴ costs should not constitute a barrier to accessing debt relief and should be shared by all stakeholders as efficient and effective insolvency systems strive to improve the adverse systemic effects of unregulated distressed debt which ultimately benefits (socially and economically) all involved.³⁶⁵

I recommend the following broad financing model that was touched upon when the different proposed procedures were discussed above.³⁶⁶ The proposed liquidation and repayment plan procedures should, in addition to costs relating to the application, be financed from the assets and income collected. This will represent the debtor's contribution. As it is proposed that a discharge should ultimately be awarded in all of the formal procedures, creditors' contributions are reflected by the discharge. As regards the proposed NINA procedure specifically, its simplified nature should result in relatively inexpensive administration.³⁶⁷ I recommend that the NCR's administration costs as regards the proposed NINA procedure should be financed by a minimal application fee payable by the debtor,³⁶⁸ by cross-subsidisation³⁶⁹ from NCR fees collected from debtors subject to the repayment plan procedure³⁷⁰ and further through taxation of credit providers who are guilty of reckless credit extension.³⁷¹ Even though creditors may transfer some of these costs to the public, it may also be an incentive to reduce the incidence of over-indebtedness and reckless credit. This suggestion is also in line with the recent reform of the compulsory affordability assessment.³⁷²

³⁶⁴ See ch 2 par 2.7.

³⁶⁵ *Ibid.*

³⁶⁶ See para 8.2.5.2, 8.2.5.3 and 8.2.5.4.

³⁶⁷ See par 8.2.5.4.

³⁶⁸ *Ibid.*

³⁶⁹ See ch 2 par 2.6.2.2.

³⁷⁰ See par 8.2.5.3.

³⁷¹ See ch 2 par 2.7 read together with ch 5 par 5.5.

³⁷² *Ibid.*

8.2.7 Non-discrimination

As non-discrimination forms an essential element of economic rehabilitation, international principles and guidelines³⁷³ suggest that discrimination on financial grounds as regards both entrance and discharge should be eliminated. Constitutional imperatives also call for non-discriminatory practices and procedures.³⁷⁴ In this respect I submit that my recommendations as regards the proposed procedures will reach these objectives.³⁷⁵ I further recommend that the stigmatising effects of insolvency procedures should be reduced, by for instance removing unnecessary and obsolete damaging restrictions, disqualifications and prohibitions whilst such procedures are in force. This will encourage the effective financial and social inclusion of debtors and their families.³⁷⁶ Once a discharge has been granted, the debtor should have full access to financial activities.³⁷⁷ It was therefore recommended that any information relating to insolvency procedures should be automatically removed from credit bureaux once the discharge becomes effective³⁷⁸ and perhaps more importantly the use of insolvency information should be prohibited once the discharge is granted.

8.2.8 Ancillary debt relief procedures

It has been established that while some legal measures might not be categorised as mainstream debt relief procedures, they could have the ancillary effect of providing assistance to debt-stricken natural persons and could potentially support mainstream measures.³⁷⁹ I recommend two reforms as regards ancillary debt relief procedures. These relate to sections 83 and 85 of the NCA.

It was seen that the section 85 procedure acts as an alternative port to a court-ordered debt restructuring in terms of the Act.³⁸⁰ It is suggested that the section remains in the NCA, but that it be amended to afford any court in which a credit agreement is considered the discretion from any procedural stance to refer the

³⁷³ Ch 2 par 2.7.

³⁷⁴ See ch 4 par 4.4.

³⁷⁵ Para 8.2.5.2, 8.2.5.3 and 8.2.5.4.

³⁷⁶ See ch 2 par 2.7.

³⁷⁷ *Ibid.*

³⁷⁸ See par 8.2.4.3.

³⁷⁹ See ch 5 par 5.9.

³⁸⁰ Ch 5 par 5.4.

consumer to any of the proposed debt relief measures³⁸¹ where it is of the opinion that the factual circumstances would meet the specific procedure's requirements and where the debtor agrees thereto. This recommendation will ensure that as many qualifying debtors as possible enter the formal procedures which will have a beneficial impact on the larger socio-economic environment. However, a relatively short fixed period should be set for the debtor to apply for formal relief and where he fails to apply within the time-frame, the referral order should automatically lapse and enforcement proceedings should continue without more.

As regards the NCA's reckless credit provisions, I recommend that the third consequence of reckless credit extension, as is set out in section 83(3), should be amended to refer to any of the proposed formal debt relief measures.³⁸²

8.3 Concluding remarks

Although South Africa has embraced the benefits of credit, its regulation of distressed debt has received little attention. As the country is enjoying the benefits of a modern credit-driven society, it is high time that it (for the benefit of all) pays principled attention to its fallout by modernising its natural person insolvency laws.

In conclusion, the words of Fletcher that highlight the necessity of natural person insolvency systems in general are particularly apt within the present worldwide economic turmoil and particularly as regards the South African socio-economic stance.³⁸³

It is a hypothetical possibility, even today, that there could exist a social system from which the phenomenon of insolvency was totally absent. If all transactions within the community, both in commercial and in private matters, took place on a strictly cash basis – or by way of barter involving simultaneous exchange – it might be supposed that no individual would ever arrive at a state in his affairs where the sum of his unsatisfied liabilities exceeded the sum of his available assets . . . In reality of course, civilised societies have for many centuries availed themselves of the additional convenience, and enhanced commercial and economic opportunities, which the creation and use of credit can impart . . . Nevertheless, the relationship of debtor and creditor has its darker aspects, and in the absence of balanced and effective legal regulation there is

³⁸¹ See para 8.2.5.2, 8.2.5.3 and 8.2.5.4.

³⁸² *Ibid.*

³⁸³ Fletcher *The law of insolvency* 3–4.

a potential for hardship and oppression to be experienced on either side. This in turn can give rise to serious social tensions and disharmony, particularly in periods of economic recession when the incidence of financial failures tends to be at its height.

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FirstRand Bank Ltd v Carl Beck Estates (Pty) Ltd and another 2009 (3) SA 384 (T)

FirstRand Bank Ltd v Evans 2011 (4) SA 597 (KZD)

FirstRand Bank Ltd v Fillis and another 2010 (6) SA 565 (ECP)

FirstRand Bank Ltd v Janse Van Rensburg and a related matter [2012] 2 All SA 186 (ECP)

FirstRand Bank Ltd v Kona case number 20003/2014 (SCA) 8

FirstRand Bank Ltd v Maleke and three similar cases 2010 (1) SA 143 (GSJ)

FirstRand Bank Ltd v Mvelase 2011 (1) SA 470 (KZP)

FirstRand Bank Ltd v Olivier 2009 (3) SA 353 (SE)

FirstRand Bank v Raheman and another 2012 (3) SA 418 (KZD)

FirstRand Bank Ltd v Smith unreported WLD case nr 24208/2008

Fortuin and others v Various Creditors 2004 (2) SA 570 (C)

G

Gardee v Dhanmanta Holdings and others 1978 (1) SA 1066 (N)

Grainco (Pty) Ltd v Broodryk NO en andere 2012 (4) SA 517 (FB)

Greub v The Master 1999 (1) SA 746 (C)

Grevler v Landsdown en 'n ander NNO 1991 (3) SA 175 (T)

Gundwana v Steko Development and others 2011 (3) SA 608 (CC)

H

Harksen v Lane 1998 (1) SA 300 CC

Hillhouse v Stott; Freban Investments (Pty) Ltd v Itzkin; Botha v Botha 1990 (4) SA 580 (W)

Horwood v FirstRand Bank Ltd unreported SGJ case nr 36853/2010

I

Investec Bank Ltd v Mutemeri and another 2010 (1) SA 265 (GSJ)

J

Jacobs v African Bank Bpk 2006 (5) SA 21 (T)

Jaftha v Schoeman and Others; Van Rooyen v Stoltz and others 2005 (2) SA 140 (CC)

Jili v FirstRand Bank Ltd t/a Wesbank [2015] JOL 32580 (SCA)

JMV Textiles (Pty) Ltd v De Chalain Spareinvest 14 CC and others 2010 (6) SA 173 (KZD)

K

Kerbel v Chames 1925 WLD 72

Kubyana v Standard Bank of South Africa Ltd 2014 (3) SA 56 (CC)

L

Levine v Viljoen 1952 (1) SA 456 (WLD)

Lion Match Co Limited v Wessels 1946 OPD 376

London Estates (Pty) Ltd v Nair 1957 (3) SA 591 (D)

LTA Construction Bpk v Administrateur Transvaal 1992 (1) SA 473 (A)

Lynn & Main Inc v Naidoo and another 2006 (1) SA 59 (N)

M

Madari v Cassim 1950 (2) SA 35 (N)

Mercedes Benz Financial Services South Africa (Pty) Ltd v Dunga 2011 (1) SA 374 (WCC)

Meskin & Co v Friedman 1948 (2) SA 555 (W)

Meyer v Batten 1999 (1) SA 1041 (W)

Mitchell v Beheerliggaam RNS Mansions 2010 (5) SA 75 (GNP)

Mnisi v Magistrate, Middelburg and others [2004] 3 All SA 734 (T)

Mthimkhulu v Rampersad and another (Boe Bank Ltd, Intervening Creditor) [2000] 3 All SA 512 (N)

Myburgh Transport v Botha t/a SA Truck Bodies 1991 (3) SA 310 (NmS)

N

Naidoo v ABSA Bank Ltd 2010 (4) SA 597 (SCA)

National Credit Regulator v Nedbank Ltd and others 2009 (6) SA 295 (GNP)

Nedbank v Andrews (240/2011) [2011] ZAECPEHC 29 (10 May 2011)

Nedbank Ltd v Binneman and thirteen similar cases 2012 (5) SA 569 (WCC)

Nedbank Ltd v Mateman and Others; Nedbank Ltd v Stringer and another 2008 (4) SA 276 (T)

Nedbank Ltd v Maxwell unreported SGJ case nr 18027/2010

Nedbank Ltd v National Credit Regulator and another 2011 (3) SA 581 (SCA)

Nedbank Ltd v Soneman and another 2013 (3) SA 526 (ECP)

Nedbank Ltd v Wizard Holdings (Pty) Ltd and others 2010 (5) SA 523 (GSJ)

Nel NO v Body Corporate of the Seaways Building and another 1996 (1) SA 131 (A)

Nelson Mandela Bay Metropolitan Municipality v Nobumba NO and others 2010 (1) SA 579 (ECG)

Newcombe v O'Brien 20 EDC 292

Nieuwenhuizen and another v Nedcor Bank Ltd [2001] 2 All SA 364 (O)

P

Phillips and others v National Director of Public Prosecutions 2003 (6) SA 447 (SCA)

President of the Republic of South Africa and another v Hugo 1997 (4) SA 1 (CC)

Pretoria City Council v Walker 1998 (2) SA 363 (CC)

Prinsloo v Van der Linde and another 1997 (3) SA 1012 (CC)

Prudential Shippers SA Ltd v Tempest Clothing Co (Pty) Ltd and others 1976 (2) SA 856 (W)

R

R v Meer and others 1957 (3) SA 614 (N)

Ribeiro and another v Slip Knot Inv 777 (Pty) Ltd 2011 (1) SA 575 (SCA)

RMB Private Bank A Division of FirstRand Bank Ltd v Kaydeez Therapies CC (in liquidation and others) 2013 (6) SA 308 (GSJ)

Rossouw and another v FirstRand Bank Ltd 2010 (6) SA 439 (SCA)

S

SA Taxi Securitisation (Pty) Ltd v Chesane 2010 (6) SA 557 (GSJ)

SA Taxi Securitisation (Pty) Ltd and two similar cases v Mbatha 2011 (1) SA 310 (GSJ)

SA Taxi Securitisation (Pty) Ltd v Ndobela (9162/2010) [2011] ZAGPJHC 14 (15 March 2011)

Schlesinger v Schlesinger 1979 (4) SA 342 (W)

Schwartz v Schwartz 1984 (4) SA 467 (A)

Sebola and another v Standard Bank of South Africa Ltd and another 2012 (5) SA 142 (CC)

Sellwell Shop Interiors v Van der Merwe unreported case number 27527/90 (W) (16 November 1990)

Seyffert and another v FirstRand Bank Ltd t/a First National Bank 2012 (6) SA 581 (SCA)

South African Police Service v Public Servants Association 2007 (3) SA 521 (CC)

Standard Bank of South Africa Ltd v Hales and another 2009 (3) SA 315 (D)

Standard Bank of South Africa Ltd v Hunkydory Investments 194 (Pty) Ltd (No1) and another 2010 (1) SA 627 (C)

Standard Bank of South Africa Ltd v Kallides unreported WCC case nr 1061/2012

Standard Bank of South Africa Ltd v Panayiotts 2009 (3) SA 363 (W)

Standard Bank of South Africa Ltd v Saunderson and others 2006 (2) SA 264 (SCA)

Stander v Erasmus and others 2011 (2) SA 320 (GNP)

Streicher v Viljoen [1999] 3 All SA 257 (NC)

Structured Mezzanine Investments (Pty) Ltd v Davids 2010 (6) SA 622 (WCC)

T

Trust Wholesalers and Woollens (Pty) Ltd v Mackan 1954 (2) SA 109 (N)

V

Van Rooyen v Van Rooyen (Automutual Investments (EC) (Pty) Ltd, Intervening Creditor) [2000] 2 All SA 485 (SE)

W

Walker v Syfret 1911 AD 141

Weiner NO v Broekhuysen 2003 (4) SA 301 (SCA)

Wepener v Erickson 1926 WLD 81

Wesbank A Division of FirstRand Bank Ltd v Martin 2012 (3) SA 600 (WCC)

Wesbank A Division of FirstRand Bank Ltd v Papier (National Credit Regulator as Amicus Curiae) 2011 (2) SA 395 (WCC)

Y

Yenson and Co v Garlick 1926 WLD 53

8.4 United States of America

Local Loan Co v Hunt 1934 292 US 234

9. MISCELLANEOUS

MODE OF CITATION

South Africa

Fin24

African Bank fined R20m for reckless lending
<http://bit.ly/Mwy8AR> (accessed 27 December 2014)

Fin24

African Bank placed under curatorship
<http://bit.ly/1reuxWp> (accessed 27 December 2014)

Fin24

African Bank kept lending to indebted customers
<http://bit.ly/1A23y7Z> (accessed 27 December 2014)

African Bank Investments Limited

African Bank fine verges on overkill <http://bit.ly/1L7EhN7>
(accessed 27 December 2014)

Fin24

African Bank fined R20m for reckless lending
<http://bit.ly/Mwy8AR> (accessed 27 December 2014)

Cosatu

Statement <http://bit.ly/1LyErgi> (accessed 23 June 2015)

Moneyweb

South Africans are the world's biggest borrowers
<http://bit.ly/1RxsTS0> (accessed 23 June 2015)